

***United States Court of Appeals  
for the Second Circuit***



**APPENDIX**





ORIGINAL

# 75-7051

## United States Court of Appeals

For the Second Circuit.

FIRST NATIONAL BANK OF HOLLYWOOD, DOROTHY BUCHMAN and SANDER BUCHMAN, as Executors of SAMUEL BUCHMAN, Deceased,

*Plaintiffs-Appellees,*

*against*

AMERICAN FOAM RUBBER CORP., MILTON R. ACKMAN, as Trustee of AMERICAN FOAM RUBBER CORP., Bankrupt,

*Defendants,*

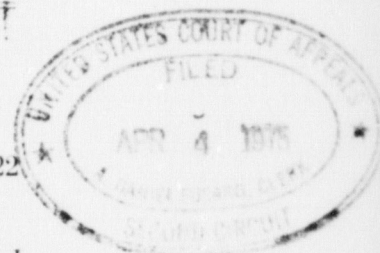
MARIE LOUISE DEMONTMOLLIN, ALEXANDER F. PATHY and SUZANNE M. PATHY,

*Defendants-Appellants.*

### JOINT APPENDIX.

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DOROTHY BUCHMAN,  
*As Executrix of the Estate of Samuel  
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UNITED STATES COURT OF APPEALS,  
FOR THE SECOND CIRCUIT.

-----X

FIRST NATIONAL BANK OF HOLLYWOOD, DOROTHY BUCHMAN AND  
SANDER BUCHMAN, as Executors of SAMUEL BUCHMAN, Deceased,

*Plaintiffs-Appellees,*

*-against-*

AMERICAN FOAM RUBBER CORP., MILTON R. ACKMAN, as Trustee  
of AMERICAN FOAM RUBBER CORP., BANKRUPT,

*Defendants,*

MARIE LOUISE de MONTMOLLIN, ALEXANDER F. PATHY and  
SUZANNE M. PATHY,

*Defendants-Appellants.*

-----X

RELEVANT DOCKET ENTRIES.

Date	PROCEEDINGS.
June 14-60	Filed complaint & issued summons
July 12-60	Filed REPLY to counterclaim.
May 16/61	Filed affdvts. Exhibit & notice of motion to permit defts', Marie Louise de Mont- mollin, & Alexander F. Pathy & Suzanne M. Pathy to file an amended & supple- mental answer, - ret. 5/23/61.
Dec 8-61	Filed Opinion #27354 granting motion permitting individual defts to serve and



## RELEVANT DOCKET ENTRIES

Date	PROCEEDINGS
	file an amended and supplemental answer containing two counterclaims - Mertzner, J. - m.n.
Dec 3/62	Filed Answer to Complaint by deft. Milton R. Ackman
Dec 22/62	Filed pltff's REPLY to answer of deft. Milton R. Ackman
Aug. 17-66	Filed MEMORANDUM OPINION #32, 646-- Pltff's motion for Summary Judgment Denied.
May 9-67	Filed memorandum Opinion # 33489 - deft's motion for summary judgment is denied - so Ordered--Cooper, J M/N
Mar. 7-68	Filed deft's Louise de Montmolin, Alex Pathy & Suzanne M. Pathy-Motion for Summary Judgment.
Apr. 17-68	Trial cont'd Jury finds conspiracy by pltff.
Dec. 3-68	Before, Cooper, J.-Non-Jury trial continued from 4-29-68-Trial as to pltffs case
Jul. 23-69	Filed Memorandum Opinion #36027--During the course of the trial, decision was reserved on a number of evidentiary rulings. Individual defts' motion to

## RELEVANT DOCKET ENTRIES

Date

## PROCEEDINGS

strike Exh. 34 is denied, objections to Exhs. 39, 41 and 42 are overruled; plttfs' motion to strike Exh, ES is denied; objections to Exhs. EV, EW, EK and EY are sustained, objection to Exh. EZ is overruled. Individual defts' motion to dismiss is denied. The parties are allowed 15 days from date of this opinion to serve and file proof in affidavit form as to remaining issue of damages, etc. As to liability only, the foregoing shall constitute this Court's findings of fact and conclusions of law. Cooper, J. m/n 52pp.

Sep. 26-69

Filed memorandum and order that entry of judgment on plttf's second cause of action must await determination of damages, we direct that judgment be entered on all other claims in this litigation. Entry of Judgment shall not be delayed for the taxing of costs. The parties shall submit forms of judgment on notice within 10 days from this date, Cooper, J.



## RELEVANT DOCKET ENTRIES

## DATE

## PROCEEDINGS

Sep. 26-69

Filed memorandum and order that the Trustee in Bankruptcy of American Foam Rubber Corp. moves to have pre-verdict interest added to the \$20,000 Jury Verdict. Accordingly, we find that the Trustee is entitled to pre-verdict interest as a matter of right. Such interest shall be computed at the rate of 6% per annum from July 1, 1959 etc. So Ordered--  
Cooper, J. m/n

Oct. 9-69

Filed Judgment #70,289-Pltffs. have judgment on 1st cause of action against American Foam Rubber Corp. in the sum of \$64,000- with interest at 5% per annum in the amount of \$1,484.47 or in all \$65,484.47, with costs to be taxed in favor of pltffs. against Amer. Foam Rubber Corp., that pltffs' second cause of action against defts. Alexander F. Pathy & Suzanne M. Pathy is dismissed with costs to be taxed in favor of said defts; that debt. Milton R. Ackman, as Trustee of Amer. Foam Rubber Corp., bankrupt, have judgment on his First Counterclaim against pltffs.

## RELEVANT DOCKET ENTRIES

DATE

## PROCEEDINGS

First National Bank, Dorothy Buchman, & A. Sander Buchman, as executors of S. Buchman, deceased, in the sum of \$20,000- with interest at 6% per annum, that debt. Ackman's 2nd counterclaim against pltffs & cross-claim against debts. Marie Louise de Montmollin, A. F. Pathy & Suzanne M. Pathy is dismissed without costs to pltffs. & with costs to be taxed without costs, etc. & as further indicated.-- Cooper, J.-Judgment ent.-Clerk

Nov. 21-74

Filed memo endorse on motion filed 10-4074--The sole issue/must be resolve on this motion for summary judgment is the amount of interest due pltff. Buchman on the \$15,000 judgment. Pltff. should be awarded simple interest on the \$15,000 judgment at the legal rate indicated. The interest computed by the judgment clerk following this formula shall be added to the award of \$26,852.58 as to which there is no dispute. So Ordered-- Cooper, J. Mailed notices.



## RELEVANT DOCKET ENTRIES

## DATE

## PROCEEDINGS

Dec. 20-74

Filed Order & Judgment #74,988--Pltff's motion for summary judgment is granted Pltff. recover of debt. Marie Louise de Montmollin the total sum of \$14,016.00 Pltff, recover of debt. Marie Louise de Montmollin the addt'l sum of \$40,868.59--Cooper, J.--Judgment Entered-Clerk.

Jan. 10-75

Filed defts' (de Montmollin & Pathy) notice of appeal from order & judgment entered 12-20-74. Mailed copies to Lorwin Goldman Gutin Rosen & Greene 540 Madison Ave. N. Y. C. and to Kleeberg & Greenwald 11 E. 44th Str. N. Y. C.

PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER.

UNITED STATES DISTRICT COURT FOR THE  
SOUTHERN DISTRICT OF NEW YORK

----- X

SAMUEL BUCHMAN,

Plaintiff,

-against-

AMERICAN FOAM RUBBER CORPORATION,  
MARIE LOUISE de MONTMOLLIN,  
ALEXANDER P. PATHY and SUZANNE M.  
PATHY,

COMPLAINT

Defendants.

----- X

Plaintiff, by his attorneys WEYMAN & NEITLICH, ESQS.,  
complaining of the defendants herein alleges:

AS AND FOR A FIRST SEPARATE AND  
DISTINCT CAUSE OF ACTION AGAINST  
DEFENDANT AMERICAN FOAM RUBBER  
CORPORATION

FIRST: Plaintiff is, and for a period of years prior to  
the institution of this action has been, a resident of and domi-  
ciled in the State of Florida.

SECOND: Defendant AMERICAN FOAM RUBBER CORPORATION  
(hereinafter sometimes referred to as "the Corporation") is a  
corporation organized and existing under and by virtue of the laws  
of the State of New York, and having its principal office at 350  
Fifth Avenue, Borough of Manhattan, City, County and State of  
New York.

THIRD: Jurisdiction of this Court is based upon the  
following: Plaintiff is a citizen of the State of Florida and



## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

defendant AMERICAN FOAM RUBBER CORPORATION is incorporated under the laws of the State of New York and has its principal office in the City and State of New York. The matter in controversy exceeds, exclusive of interest and costs, the sum of \$10,000.00.

✓ FOURTH: On or about August 1, 1955, the corporation issued to the plaintiff thirty-four (34) of the Corporation's "Series B" debentures, each of which said debentures is dated August 1, 1955, payable August 1, 1965, in the face amounts thereof to the registered holder thereof, with interest at 5% per annum. The aggregate of the face amounts of said debentures is \$64,000.00. A photostatic copy of one of said

debentures is annexed hereto as Exhibit "A" and made a part hereof. Each of the said thirty-four (34) debentures issued by the Corporation to the plaintiff is in form identical to Exhibit "A", except for its face amount.

FIFTH: At all times hereinmentioned plaintiff was and still is the registered holder of the aforementioned thirty-four (34) Series B debentures of the Corporation, having an aggregate face value of \$64,000.00.

## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

FIFTH A: The Corporation paid plaintiff interest under and as prescribed by said debentures to and including the interest which fell due August 1, 1960, but paid no part of the principal.

FIFTH B: On January 17, 1961, the Corporation filed a voluntary petition for an arrangement under Chapter XI of the Bankruptcy Act of the United States.

FIFTH C: On February 21, 1961, the Corporation was on said petition duly adjudicated a bankrupt in the United States District Court for the Southern District of New York; and on February 23, 1961, Milton R. Ackman was appointed Trustee in Bankruptcy of the Corporation and he has at all times since been and now is acting as such Trustee.

FIFTH D: By reason of the foregoing, there became due and payable by American Foam Rubber Corporation, bankrupt, to the plaintiff the sum of \$64,000.00, with interest at 5% per annum from August 1, 1960 to January 17, 1961, no part of which has been paid to the plaintiff although duly demanded.



## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

SIXTH: Each of the aforementioned 64 debentures provides, among other things, as follows:

"4. Interest shall be paid to the registered holder by check mailed to him at the address appearing upon said register semi-annually on the first days of February and August of each year.

5. Commencing on February 1, 1956 and on each interest payment date thereafter, the undersigned will make payment by like check to the registered holders of said debentures of five percent (5%) of the respective principal amounts thereof. The undersigned shall, however, not be required to make any payment on account of principal if the undersigned has not accumulated earnings and profits at least sufficient in amount to provide for that payment. The undersigned agrees that as long as any past due instalments of principal remain unpaid it will not declare any dividends upon any class of its capital stock and that instalments of principal previously unpaid shall be made good out of the first accruing earnings and profits from which such payments may be made. The words 'earnings and profits' as used in this paragraph shall mean accumulated profits less all taxes, dividends and payments on account of principal of said debentures."

SEVENTH: The Corporation has failed, neglected and refused to make any payments on account of the principal of the said debentures although such payments have been duly demanded.

EIGHTH: Upon information and belief, the corporation has had accumulated earnings and profits sufficient in amount to provide for the instalment payments due February 1, 1956 and on each interest payment date thereafter, up to and including February 1, 1960, in accordance with Paragraph "5" of the said debentures.

NINTH: By reason of the foregoing there became due and payable by the Corporation to the plaintiff as at February 1, 1960 nine (9) instalments, each in the amount of five (5%) per centum

## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

of the face amount of the aforementioned debentures, totaling in all the sum of \$28,800.00, no part of which has been paid to the plaintiff although duly demanded.

AS AND FOR A SECOND SEPARATE AND  
DISTINCT CAUSE OF ACTION AGAINST  
DEFENDANTS MARIE LOUISE de MONT-  
HOLLIN, ALEXANDER F. PATHY AND  
SUZANNE M. PATHY

TENTH: Plaintiff repeats and realleges each and every allegation set forth in paragraphs "FIRST", "SECOND", "FOURTH", "FIFTH", "SIXTH", "SEVENTH", "EIGHTH" and "NINTH" of the complaint with the same force and effect as if herein set forth in full.

ELEVENTH: Upon information and belief, the aforementioned individual defendants, MARIE LOUISE de MONTMOLLIN, ALEXANDER F. PATHY and SUZANNE M. PATHY, and each of them, are citizens and/or residents of the State of New York, and none of said defendants is a citizen or resident of the State of Florida.

TWELFTH: Jurisdiction of this Court is based upon the following: Plaintiff is a citizen of the State of Florida; the individual defendants are citizens and/or residents of the State of New York; the amount in controversy in this matter exceeds the sum of \$10,000.00.

THIRTEENTH: On or about May 17, 1957, plaintiff and the three above-named individual defendants entered into an agreement in writing wherein and whereby the aforementioned three individual defendants agreed to purchase and did purchase from the plaintiff all of the shares of the capital stock held by the plaintiff in AMERICAN FOAM RUBBER CORPORATION and in another corporation known as BURLINGTON HOLDING CORP.



## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

FOURTEENTH: Paragraph "SIXTH" of the aforesaid agreement of May 17, 1957 provides as follows:

"SIXTH: Subordination

A. The parties named below hold five (5%) percent registered debentures issued by American Foam or Burlington in the following respective amounts:

<u>Name of Holder</u>	<u>American Foam Series A Debenture Due May 1, 1960</u>	<u>American Foam Series B Debenture Due May 1, 1965</u>	<u>Burlington Debenture Due April 1, 1960</u>
Samuel Buchman	\$48,000	\$64,000	\$12,000
Marie Louise de Montmollin	63,000	79,000	15,000
Alexander F. Pathy	-0-	50,000	-0-

To induce Samuel Buchman to sell his capital stock hereunder, Marie Louise de Montmollin and Alexander F. Pathy hereby agree with respect to the debentures of each of said corporations that the rights of any holder (including her or him) of the debentures thereof now held by her or him and referred to above, be subordinated to the rights of any holder or holders of the debentures thereof now held by Samuel Buchman (including him) as to the payment of interest and principal. No claim for interest under the debentures so subordinated shall be made unless all interest payable on the debentures now held by Samuel Buchman shall have been paid in full, and no claim for principal under any of the debentures so subordinated shall be made unless the entire principal of all the debentures now held by Samuel Buchman shall have been paid in full.

✓ If for any reason, either corporation shall pay interest or principal on said debentures to any of the Buyers, or to any person deriving title to the debentures of said corporation from any of the Buyers, and said payment shall be made without first satisfying the priority to which the holder or holders of Samuel Buchman's debentures are entitled by reason of the foregoing provisions, the amount or amounts of the payment so made to the Buyer (or to the person deriving title from her or him) shall be promptly paid by such Buyer to said holder or holders of Samuel Buchman's debentures. Any payment made on account of principal shall be endorsed on said debentures, which shall be submitted to the payor for that purposes.

## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

"B. Samuel Buchman is the holder of a five (5%) percent Promissory Note of American Foam in the sum of \$25,000. The Buyers hold similar Promissory notes aggregating \$100,000. To induce Samuel Buchman to sell his capital stock hereunder, the Buyers hereby agree to subordinate the payment of (1) interest of their respective said Promissory Notes to the payment of interest and (2) principal thereof to the payment of principal, on or of said \$25,000 Promissory Note held by Samuel Buchman and they further agree to make no claim for interest on their respective said Promissory Notes until interest on the Promissory Note held by Samuel Buchman shall have been paid in full, and to make no claim for principal unless the principal of the Promissory Note held by Samuel Buchman shall have been paid in full.

C. To induce the respective Buyers to buy his capital stock sold hereunder, Samuel Buchman hereby agrees with respect to his debentures of American Foam and Burlington that the rights of any holder (including him) of said debentures shall in all respects continue to be subordinated, as they are presently, to claims of The First Pennsylvania Banking and Trust Company now existing against said corporations or either of them by reason of credit extended, or to claims of any other financial institution which after the date hereof may in whole or in part become a creditor of said corporations or either of them by reason of the refinancing of the credit now extended to said corporations or either of them by The First Pennsylvania Banking and Trust Company. Samuel Buchman's agreement so to continue the subordination of his debentures shall be subject to the two following limitations: (1) Such agreement shall expire on December 31, 1959, and (2) the aggregate indebtedness of either or both of said corporations to which his debentures shall continue to be subordinated, as above provided, shall not be in excess of \$650,000."

FIFTEENTH: On or about May 1, 1960, the AMERICAN FOAM RUBBER CORPORATION "Series A" debentures referred to in paragraph "SIXTH" of the May 17, 1957 agreement, then held by the plaintiff, and having an aggregate face value of \$48,000.00 were paid and retired by the Corporation.

SIXTEENTH: Upon information and belief, the three named individual defendants are, and at all times herein mentioned were,



## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

the officers, directors and sole stockholders of AMERICAN FOAM RUBBER CORPORATION and were and still are in full operating management and control of said corporation.

SEVENTEENTH: Upon information and belief, on or about June 1, 1957, the defendant, Alexander F. Pathy, sold to the defendant, Marie Louise de Montmollin, his "Series B" debentures in the Corporation for the sum of \$80,000.00 and received such amount from her in payment therefor.

Upon information and belief, in or about April or May 1958, the three individual defendants in their capacities as officers, directors and stockholders of American Foam Rubber Corporation, and also as the holders of both "Series A" and "Series B" debentures of said Corporation, caused the said Corporation to amend its Certificate of Incorporation so as to provide for 3,500 shares of 5% cumulative preferred stock of the Corporation, and thereupon the three individual defendants in their capacities as officers, directors and stockholders of American Foam Rubber Corporation caused said Corporation to issue to themselves shares of said preferred stock in exchange for and in payment of the aforementioned "Series A" and "Series B" debentures theretofore held by the individual defendants.

## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

Upon information and belief, that in or about April 1960, the individual defendants in their capacities as officers, directors and stockholders of American Foam Rubber Corporation, and as directors and officers of Burlington Holding Corporation, the subsidiary of American Foam Rubber Corporation, caused the defendant Marie Louise de Montmollin to be credited on the books of Burlington Holding Corporation with the receipt of \$15,000.00 and the simultaneous discharge of \$15,000.00 of Burlington debentures then held by her, and the said Marie Louise de Montmollin then simultaneously loaned the said sum of \$15,000.00 to American Foam Rubber Corporation which the individual defendants in their capacities as officers, directors and stockholders of American Foam Rubber Corporation accepted from her as such loan.

"Series B" debentures of said Corporation, caused the said corporation to issue shares of the preferred stock of said Corporation to themselves, in exchange for and in payment of the aforementioned "Series A" and "Series B" debentures then held by the individual defendants, MARIE LOUISE de MONTMOLLIN and ALEXANDER F. PATHY.

EIGHTEENTH: By reason of the foregoing, the defendants MARIE LOUISE de MONTMOLLIN and ALEXANDER F. PATHY have received



## PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

payment of the amounts due on the debentures held by them in the Corporation, but the said defendants have failed to make an equivalent payment to the plaintiff herein of the amounts received by them, sufficient to retire or purchase the Series B debentures held by plaintiff in the aggregate amount of \$64,000.00.

NINETEENTH: By reason of the foregoing, the aforementioned defendants MARIE LOUISE de MONTMOLLIN and ALEXANDER F. PATHY have received payment of the amounts due on the debentures of the Corporation held by them, without satisfying the priority to which plaintiff was entitled in the payment of his debentures, all in breach and violation of the agreement between and among the parties.

TWENTIETH: By reason of the foregoing, plaintiff has been damaged in the amount of \$64,000.00 with interest from May 1, 1960.

WHEREFORE, plaintiff demands judgment as follows:

(A.) Against the defendant American Foam Rubber Corporation in the amount of \$64,000.00, with interest at 5% per annum from August 1, 1960 to January 17, 1961.

(B.) Against the individual defendants Marie Louise de Montmollin, Alexander F. Pathy and Suzanne M. Pathy, jointly and severally in

PLAINTIFF'S COMPLAINT AS AMENDED BY THE PRE-TRIAL ORDER

the amount of \$64,000.00, with interest from  
June 1, 1957.  
together with the costs and disbursements of this action as provided by law.

WHITMAN AND NEITLICH  
Attorneys for Plaintiff

By:

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AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
BY THE PRE-TRIAL ORDER.

UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK

SAMUEL BUCHMAN,

Plaintiff,

-against-

AMERICAN FOAM RUBBER CORPORATION,  
MARIE LOUISE de MONTMOLLIN,  
ALEXANDER F. PATHY and SUZANNE M.  
PATHY,

Defendants.

Civil Action  
No. 60 Civ. 2328

AMENDED AND  
SUPPLEMENTAL  
ANSWER

Defendants, MARIE LOUISE de MONTMOLLIN, ALEXANDER  
F. PATHY and SUZANNE M. PATHY, (hereinafter sometimes  
referred to as the "Answering Defendants"), by their  
attorneys, Winer, Neuburger & Sive, Esqs., for their  
Amended and Supplemental Answer to the Complaint herein,  
allege as follows:

1. The Answering Defendants deny knowledge or  
information sufficient to form a belief as to the truth of  
the allegations contained in paragraphs "FIRST" and "TWELFTH"  
of the complaint.

2. The Answering Defendants deny each and  
every allegation contained in paragraphs "SEVENTH", "EIGHTH",  
"NINTH", SEVENTEENTH", "EIGHTEENTH", "NINETEENTH", and

AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
BY THE PRE-TRIAL ORDER

"TWENTIETH" except that they admit with respect to paragraph "SEVENTEENTH" that they did exchange certain debentures then held by them for subordinated preferred stock of defendant AMERICAN FOAM RUBBER CORPORATION.

3. The Answering Defendants admit the allegations of paragraph "SIXTEENTH" of the complaint, except that they deny that at all times mentioned in the complaint they were in full operating management and control of defendant AMERICAN FOAM RUBBER CORPORATION.

AS AND FOR A FIRST AFFIRMATIVE DEFENSE

4. The complaint fails to state a claim against defendants upon which relief can be granted.

AS AND FOR A SECOND AFFIRMATIVE DEFENSE

5. Plaintiff had knowledge of the exchange of the defendants' debenture for preferred stock at or about the date of said exchange. Plaintiff acquiesced and consented to the said exchange.

AS AND FOR A FIRST COUNTERCLAIM AND  
A THIRD AFFIRMATIVE DEFENSE



AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
BY THE PRE-TRIAL ORDER

6. Upon information and belief, defendant American Foam Rubber Corporation (hereinafter sometimes referred to as "AFR Corp.") was organized by plaintiff Buchman in March 1950, and from the date of its organization and until May 17, 1957 plaintiff Buchman was the President and Chief Executive Officer of and one of three members of the Board of Directors of AFR Corp. At various times after its organization, AFR Corp. caused to be created and organized and acquired all of the capital stock of various subsidiary corporations. (AFR Corp. and the said subsidiaries are hereinafter sometimes referred to collectively as "AFR Group").

7. Upon information and belief, between the date of its organization and February 21, 1961, when AFR Corp. was adjudged a bankrupt in proceedings in this Court, in Bankruptcy, bearing index number 61-B-35, AFR Corp. was engaged in the business of the manufacture and sale of foam rubber, rubber mattresses and pillows, and other articles made of foam rubber, and related products, for industrial and consumer use.

8. Upon information and belief, Burlington Holding Corporation (hereinafter referred to as "Burlington")

AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
BY THE PRE-TRIAL ORDER

was organized by plaintiff Buchman in March 1950, under the laws of the State of New York, and has at all times since its organization been the owner of certain factory premises located in Burlington, New Jersey, leased to defendant AFR Corp. for its manufacturing operations. In 1958, defendant AFR Corp. acquired all of the capital stock of Burlington and Burlington thereby became and has at all times since been a wholly owned subsidiary of AFR Corp.

9. (a) At all times since 1953 defendant Alexander F. Pathy has been a Director and Officer of AFR Corp.;

(b) at all times since 1954 defendant Marie Louise de Montmollin has been a Director and Officer of AFR Corp.; and

(c) at all times since 1957 defendant SUZANNE M. PATHY has been a Director and Officer of AFR Corp.

(d) between June 30, 1954 and August, 1955, approximately 60% of the common stock of AFR Corp. was owned by the Answering Defendants and approximately 40% was owned by plaintiff Buchman and his son, A. Sander Buchman.

(e) between August, 1955 and May 17, 1957, approximately 66 2/3% of the common stock of AFR Corp. was



AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
BY THE PRE-TRIAL ORDER

owned by the Answering Defendants and approximately 33 1/3% was owned by plaintiff Buchman and his son, A. Sander Buchman.

10. Upon information and belief, between January 1, 1953 and May 17, 1957, the business, ~~as of~~, net worth, profits and prospects for future growth and profits of AFR Corp. greatly developed, expanded and appreciated.

11. Upon information and belief, from September 1956, or thereabouts, to May 17, 1957, the business operations of AFR Group were substantially divided into two divisions, to wit, the Industrial Division, concerned with the sale of articles made of foam rubber to manufacturers of foam rubber products for use in such manufacturing, and the Retail Division, concerned with the sale to wholesalers and retailers of finished articles made of foam rubber.

12. Upon information and belief, by virtue of the foregoing, and his own and his son's holdings of capital stock and debentures of AFR Corp., the offices of AFR Corp. and Burlington occupied by him since 1950, and his active charge of all of the operations and personnel, plaintiff Buchman had, on May 17, 1957;

AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
BY THE PRE-TRIAL ORDER

(a) an intensive, special and unique knowledge of and acquaintance with the business operations, affairs, transactions and assets of AFR Corp. and its subsidiaries;

(b) a close, special, unique and confidential relationship with all of the sales and other personnel employed by AFR Corp. and its subsidiaries, and was in a position to exercise substantial influence over all of the said personnel.

13. Upon information and belief, on May 17, 1957, and for the entire period of time prior thereto and during which the AFR Group had operated its Industrial Division substantially all of the sales by the Industrial Division of AFR Corp. were handled and effected by Regional Sales Representatives, including the following, who are sometimes hereinafter referred to as the Key Sales Personnel of AFR Corp.:

Louis Levy, for the Metropolitan New York  
City Area

Irving Mirsky for the Philadelphia and the  
New England Area

Donald B. Parker, for the Area of Ohio,  
Pennsylvania and several adjoining and  
nearby states

Hellmut R. Spitzer, for the Midwest Area



AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
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From its establishment to May, 1957, approximately 75% of the total sales by the Industrial Division of the AFR Group were represented by sales made by the Key Sales Personnel; the above named Louis Levy, Irving Mirsky and Donald B. Parker accounted for 60% of the said total sales.

14. On or about May 17, 1957, plaintiff Buchman and his son, A. Sander Buchman, as Sellers, and the Answering Defendants, as Buyers, entered into an agreement in writing providing for the sale by plaintiff Buchman and his son, A. Sander Buchman, to the Answering Defendants of 12,772 shares of the Class A capital stock of AFR Corp. and 30 shares of the capital stock of Burlington, constituting all of the shares of the said corporations owned by plaintiff Buchman, and 5,500 shares of the Class A capital stock of AFR Corp., constituting all of the shares of the capital stock of AFR Corp. owned by A. Sander Buchman, to the Answering Defendants, in the following proportions:

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<u>Buyer</u>	<u>Shares</u> <u>American Foam Rubber</u>
Marie Louise de Montmollin	9,161
Suzanne M. Pathy	6,871
Alexander F. Pathy	<u>2,290</u>
Total.....	18,322

15. The said agreement provided, among other things, that:

(a) The total purchase price for the said shares of stock was \$223,220.00, of which \$60,000 was payable and was paid on May 17, 1957, and the balance was payable in five installments on January 2, 1958, April 2, July 2, October 2, 1958 and on January 2, 1959.

(b) The obligations of the buyers were evidenced by a series of promissory notes, the payment of which was secured by the deposit with the attorney for the Sellers, in escrow, of all of the shares of stock purchased.

(c) Plaintiff Buchman would resign forthwith as director and officer of AFR Corp. and of Burlington and of any and all subsidiaries of AFR Corp.

16. Thereafter, and pursuant to the said agreement of May 17, 1957:



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(a) The Answering Defendants did, on May 17, 1957, pay to plaintiff Buchman and his son, A. Sander Buchman, \$60,000.00, and did make and deliver to plaintiff Buchman and his son, A. Sander Buchman, a series of promissory notes provided for in the said agreement and did deposit with the attorney for the seller, in escrow, all of the shares of stock purchased;

(b) the Answering Defendants thereafter paid the said promissory notes;

(c) the Answering Defendants in all other respects fully performed and discharged all of the terms and conditions of the said agreement of May 17, 1957 to be performed on their part;

(d) plaintiff Buchman resigned as director and officer of AFR Corp., Burlington and all subsidiaries of AFR Corp.

17. Upon information and belief, on or about May 17, 1957, or at some time shortly thereafter, the precise date of which the Individual Defendants are unable to fix, in flagrant breach and violation of his direct and separate duties and obligations to the Individual Defendants, both under the terms and

AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
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provisions of the said agreement of May 17, 1957, and arising out of the said deposit and pledge of the shares of capital stock of AFR Corp. and of Burlington sold by Buchman to the Individual Defendants and the prior relationships of the parties hereinbefore described, and with the intent to violate the same, plaintiff Buchman conceived, devised, entered upon and commenced to effect a willful, malicious, fraudulent and unlawful scheme, design and plan (hereinafter sometimes referred to as the "scheme") to:

(a) render valueless or radically impair or depreciate the value of the capital stock of AFR Corp. and Burlington sold by plaintiff Buchman and his son, A. Sander Buchman, to the Answering Defendants in and by the Agreement of May 17, 1957, as well as the shares of capital stock of AFR Corp. and Burlington theretofore held and owned by the Answering Defendants;

(b) force AFR Corp. into a condition of insolvency and bankruptcy; and

(c) acquire for himself substantially all of the assets, business and goodwill of AFR Corp., Burlington and the subsidiaries



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of AFR Corp., at a price and for a consideration amounting to only a small fraction of their actual worth in the absence of plaintiff Buchman's scheme;

by the following, among other, means and methods:

(a) corruptly and with intent to do so and without the knowledge or consent of AFR Corp. or of its officers or directors, influencing and conspiring with the Key Sales Personnel and other personnel of AFR Corp. to violate and breach their duties and obligations to AFR Corp., by offering, promising and giving to said personnel present and future gifts and gratuities;

(b) enticing away from their employment by AFR Corp. its Key Sales and other Personnel;

(c) defaming, slandering and libeling the business and financial reputation and standing of and products manufactured and sold by AFR Corp.;

(d) misrepresenting to other persons, firms and corporations doing business with, under contracts with, and having substantial

AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
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business relationship with, AFR Corp., its ability to manufacture foam rubber and foam rubber products, and to serve the needs and fulfill the orders of its customers; and

(e) obtaining from employees of AFR Corp. secret and confidential data and information and disclosing the same to competitors of AFR Corp.

18. Upon information and belief, thereafter and pursuant to his scheme;

(a) plaintiff Buchman explained and disclosed his scheme to AFR Corp.'s Key Sales Personnel and solicited and secured their joining, cooperating and participating with him in the operation and furtherance of said scheme by offering and promising to each of them a fractional share and interest in the tangible and intangible assets of AFR Corp. and its subsidiaries to be acquired under and pursuant to plaintiff Buchman's scheme and in all other unlawful benefits to be acquired by said scheme;

(b) plaintiff Buchman offered and promised to each of the said Key Sales Personnel that he would, after acquiring control and ownership of the tangible and intangible



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assets of AFR Corp. and its subsidiaries operate the same for a period of five years at a nominal salary employ each of the said Key Sales Personnel upon terms and conditions and at compensations substantially more generous and favorable than those under which they were then employed by AFR Corp.;

(c) plaintiff Buchman corruptly influenced three of the four said Key Sales Personnel, to wit, Levy, Mirsky and Parker, without the knowledge or consent of AFR Corp., or of its officers or directors, and solicited and requested them to join in a combination and conspiracy with him in furtherance of his scheme, and said Levy, Mirsky and Parker did, in fact, conspire and agree with plaintiff to do so, and in furtherance of both the scheme and conspiracy, plaintiff and said three Key Sales Personnel jointly and respectively did the following things, among others:

(1) substantially reduced their sales efforts and deliberately held down to minimal amounts the sales made by them in their respective territories, and diverted substantial amounts of sales and business from AFR Corp. to competitors of AFR Corp.;



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(2) attempted to induce and procure Spitzer by threats and corrupt inducements to similarly reduce his sales efforts in his sales territory and divert substantial amounts of sales and business from AFR Corp. to competitors of AFR Corp.;

(3) obtained from other employees and from the files and records of AFR Corp. and its subsidiaries secret and confidential information and data concerning its business, assets, liabilities and finances and to disclose the same to competitors of AFR Corp.;

(4) broadcasted and spread among other employees of AFR Corp. and its subsidiaries false rumors of the imminent failure and collapse of the business of AFR Corp. and of its imminent insolvency and bankruptcy and persuaded the said other employees to terminate their employment with AFR Corp. and its subsidiaries;

(5) dissuaded prospective employees of AFR Corp. and its subsidiaries from entering into the employ of AFR Corp. and its subsidiaries;

(6) broadcasted and spread destructive rumors and reports in the foam rubber industry and trade and elsewhere

AMENDED AND SUPPLEMENTAL ANSWER OF APPELLANTS AS AMENDED  
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of the imminent collapse of the business and insolvency and bankruptcy of AFR Corp. to impair its credit and bring it into disrepute with its customers and prospective customers.

(7) in diverse other ways, and in breach of their fiduciary obligations to AFR Corp., actively and gravely injured the business, credit, reputation and standing of AFR Corp.

(d) plaintiff Bushman induced and directed Levy, Mirsky and Parker to, and Levy, Mirsky and Parker did resign on or about March 30, 1958, from and terminate their employment by AFR Corp. and enter into employment in substantially the same sales capacities and territories with a competitor of AFR Corp., disclose secret and confidential trade information and data of AFR Corp. to said competitor and commence to assist such competitor in securing the business and customers of the Industrial Division of AFR CORP.

(e) at various times since March 30, 1958, Levy, Mirsky and Parker have worked for a competitor of AFR Corp., and have continued to disclose secret and confidential information and data of AFR Corp. to said competitor, and continued to assist such competitor in securing the business and customers of the Industrial Division of AFR Corp.



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19. By virtue of the foregoing:

(a) Sales of the territories of Levy, Mirsky and Parker of the Industrial Division of AFR Corp. were reduced as follows:

<u>Year</u>	<u>Sales</u>
1957	\$ 2,350,667.37
1958	1,114,493.44
1959	702,901.90
1960	Under \$400,000.00

(b) the capital stock of AFR Corp. and Burlington, purchased by the Answering Defendants from plaintiff Buchman, and his son, A. Sander Buchman, pursuant to the agreement of May 17, 1957, and all of the said capital stock held theretofore and purchased thereafter by the Answering Defendants, were reduced in value by no less than \$500,000.00.

(c) AFR Corp. has been rendered insolvent and adjudged bankrupt.

(d) debentures issued by AFR Corp. and Burlington to and purchased from AFR Corp. and Burlington by the Answering Defendants, in the aggregate amount of \$237,000.00, have been rendered valueless;

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(e) the Answering Defendants have suffered substantial damages owing to the loss of past and future compensations and profits;

(f) the business reputations and standing of the Answering Defendants have been seriously impaired.

AS AND FOR A SECOND COUNTERCLAIM AND A  
FOURTH AFFIRMATIVE DEFENSE

20. The Answering Defendants repeat and reallege each and every allegation contained in paragraphs "6", "7", "8" and "9" with the same force and effect as if herein fully set forth and repeated.

21. Upon information and belief, between January 1, 1953 and May 1, 1957, the business, assets, net worth, profits and prospects for future profits of AFR Corp. greatly developed, expanded and appreciated.

22. Upon information and belief, from September 1956, or thereabouts, to May 1, 1957, the business operations of AFR Group were substantially divided into two divisions, to wit, the Industrial Division, concerned with the sale of articles made of foam rubber to manufacturers of foam rubber products for use in such



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manufacturing, and the Retail Division, concerned with the sale to wholesalers and retailers of finished articles made of foam rubber.

23. Upon information and belief, by virtue of the foregoing, and his own and his son's holdings of capital stock and debentures of AFR Corp., the offices of AFR Corp. and Burlington occupied by him since 1930, and his active charge of all of the operations and personnel, plaintiff Buchman had, on May 1, 1957:

(a) an intensive, special and unique knowledge of and acquaintance with the business operations, affairs, transactions and assets of AFR Corp. and its subsidiaries;

(b) a close, special, unique and confidential relationship with all of the sales and other personnel employed by AFR Corp. and its subsidiaries, and was in a position to exercise substantial influence over all of the said personnel.

24. Upon information and belief, on May 1, 1957, and for the entire period of time prior thereto and during which the AFR Group had operated its Industrial Division substantially all of the sales by the Industrial Division of

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AFR Corp. were handled and effected by Regional Sales Representatives, including the following, who are sometimes hereinafter referred to as the Key Sales Personnel of AFR Corp.

Louis Levy, for the Metropolitan New York  
City Area,  
Irving Mirsky for the Philadelphia and the  
New England Area  
Donald B. Parker, for the Area of Ohio,  
Pennsylvania and several adjoining and  
nearby states  
Hellmut R. Spitzer, for the Midwest Area

From its establishment to May, 1957, approximately 75% of the total sales by the Industrial Division of the AFR Group were represented by sales made by the Key Sales Personnel the above named Louis Levy, Irving Mirsky and Donald B. Parker accounted for 60% of the said total sales.

23. In or about May 1957, plaintiff Buchman negotiated with the Answering Defendants for the sale of all of the shares of capital stock of AFR Corp. and Burlington owned by him and by his son, A. Sander Buchman. In the course of and in connection with the said negotiations, plaintiff Buchman represented to the Answering Defendants that:

(a) no material adverse change in the financial condition of the AFR Group had occurred between Decem-



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ber 31, 1956 and May 1, 1957 affecting the business, property and assets or net worth of the AFR Group; and

(b) no material adverse change was in prospect or in contemplation which affected the business property, assets or net worth of AFR Corp. and its subsidiaries;

(c) the plaintiff Buchman knew of no fact or circumstance adversely affecting or which would adversely affect the said business property, assets or net worth of AFR Corp. and its subsidiaries not set forth in its financial statement.

(d) plaintiff Buchman's then intent and plan was that, upon and after the sale of his and his son's shares of stock to the Answering Defendants, to have no further interest or concern with the business, property or assets of AFR Corp. or its subsidiaries except the payment of debentures owned by him and the enforcement of all his rights and claims under the contract for the sale of his shares of stock then being negotiated.

26. Upon information and belief, that such of the said representations thus made by plaintiff Buchman was false and that in truth the fact was that on or about May 1, 1957, plaintiff Buchman

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had conceived, devised, entered upon and commenced to effect and carry out and was then effecting and carrying out a willful, malicious, fraudulent and unlawful scheme, design and plan (hereinafter sometimes referred to as the "scheme") to:

(a) render valueless or radically impair or depreciate the value of the capital stock of AFR Corp. and Burlington sold by plaintiff Buchman and his son, A. Sander Buchman, to the Answering Defendants in and by the Agreement of May 17, 1957, as well as the shares of capital stock of AFR Corp. and Burlington theretofore held and owned by the Answering Defendants;

(b) force AFR Corp. into a condition of insolvency and bankruptcy; and

(c) acquire for himself all of the assets, business and goodwill of AFR Corp., Burlington and the subsidiaries of AFR Corp. at a price and for a consideration amounting to only a small fraction of their actual worth, in the absence of plaintiff Buchman's scheme;

by the following, among other, means and methods:

(a) corruptly and with intent to do so and without the knowledge or consent of



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AFR Corp. or its officers or directors, influencing the Key Sales Personnel and other personnel of AFR Corp. to violate and breach their duties and obligations to AFR Corp. by offering, promising and giving to said personnel present and future gifts and gratuities;

(b) enticing away from their employment by AFR Corp. its Key Sales and other personnel;

(c) defaming, slandering and libeling the business and financial reputation and standing of and products manufactured and sold by AFR Corp.;

(d) misrepresenting to other persons, firms and corporations doing business with, under contracts with, and having substantial business relationships with, AFR Corp., its ability to manufacture foam rubber and foam rubber products, and to serve the needs and fulfil the orders of its customers; and

(e) obtaining from employees of AFR Corp. secret and confidential data and information and disclosing the same to competitors of AFR Corp.

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27. Upon information and belief, that each of the said representations so made by plaintiff Buchman was known by him to be false when made and was made with intent to injure and defraud the Answering Defendants and to entice them to enter into an agreement with plaintiff Buchman and his son, A. Sander Buchman, for the purchase by the Answering Defendants of all of the shares of capital stock of AFR Corp. and Burlington owned by plaintiff Buchman and his son, A. Sander Buchman.

28. Upon information and belief, that the Answering Defendants, at the time such representations were made, did not know the truth but believed the said representations to be true and relied upon them and were thereby induced to make and enter into an agreement for the purchase by them of and to purchase all of the capital stock of AFR CORP. and Burlington owned by plaintiff Buchman and his son, A. Sander Buchman.

29. Upon information and belief, thereafter and in reliance upon the said representations made by plaintiff Buchman to the Answering Defendants, the Answering Defendants entered into an agreement to buy and did buy from plaintiff Buchman, 12772 shares of the Class A capital stock of AFR



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Corp. and 30 shares of the capital stock of Burlington,  
and from A. Sander Buchman, the son of plaintiff Buchman,  
5,500 shares of the Class A capital stock of AFR Corp.  
for a total purchase price of \$223,220.

30. The Answering Defendants repeat and reallege  
each and every allegation contained in paragraphs "18" and  
"19" with the same force and effect as if herein fully set  
forth and repeated.

WHEREFORE the Answering Defendants demand judgment  
dismissing the complaint herein and judgment on their  
counterclaims against plaintiff Buchman in the amount of  
\$2,000,000.00, together with exemplary damages in the amount  
of \$1,000,000.00, together with the costs and disbursements  
of this action.

SELIGSON, MORRIS & NEUBURGER  
Attorneys for Defendants  
MARIE LOUISE de MONTMOLLIN,  
ALEXANDER F. PATHY and  
SUZANNE M. PATHY  
Office & Post Office Address  
350 Fifth Avenue  
New York 1, N.Y.

ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
AMERICAN FOAM RUBBER CORPORATION, BANKRUPT ("TRUSTEE"),  
AS AMENDED BY PRE-TRIAL ORDER.

UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK

-----x

SAMUEL BUCHMAN,

Plaintiff,

- against -

Civil Action

AMERICAN FOAM RUBBER CORPORATION,  
MILTON R. ACKMAN, as Trustee of  
American Foam Rubber Corporation,  
Bankrupt, MARIE LOUISE de MONTMOLLIN,  
ALEXANDER P. PATHY and SUZANNE M.  
PATHY,

No. 60 Civ. 2323

Answer

Defendants.

-----x

Defendant MILTON R. ACKMAN, as Trustee of defendant  
American Foam Rubber Corporation, Bankrupt, by his attorneys,  
Kleeberg & Greenwald, for his answer to the complaint herein,  
alleges as follows, doing so except for paragraphs "1" and "3"  
below on information and belief:

FIRST COUNTERCLAIM

2a. Plaintiff is a citizen of the State of Florida,  
Defendant American Foam Rubber Corporation is a corporation  
incorporated under the laws of the State of New York having  
its principal place of business in that State. This answering  
defendant is a citizen of the State of New York. The matter  
in controversy exceeds, exclusive of interest and costs, the  
sum of \$10,000.

3. On January 17, 1961, defendant American Foam  
Rubber Corporation, named in the complaint, hereinafter



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referred to as "AFR", filed a voluntary petition for an arrangement under Chapter XI of the Bankruptcy Act. Thereafter and on or about February 21, 1961, AFR was duly adjudged bankrupt. On February 23, 1961, Milton K. Ackman was duly appointed Trustee in Bankruptcy of AFR and he thereupon qualified to act and has at all times since been and now is acting as such trustee and he has been duly authorized to prosecute this cause. Hereinafter said trustee is referred to as "Ackman".

4. AFR is a corporation organized and existing under and by virtue of the laws of the State of New York.

5. At all times between the date of its organization and February 21, 1961, AFR was engaged in the manufacture and sale of foam rubber, rubber mattresses and pillows, and other articles made of foam rubber, and related products, for industrial and consumer use and conducted its operations through various departments or divisions, some of them incorporated subsidiaries, the stock of which was wholly owned by AFR.

6. AFR was organized by plaintiff in March 1950 and, from the date of its organization and until on or about May 17, 1957, plaintiff was its President, Chief Executive

ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
AMERICAN FOAM RUBBER CORPORATION, BANKRUPT ("TRUSTEE"),  
AS AMENDED BY PRE-TRIAL ORDER

Officer and one of three members of its Board of Directors and, during said period, occupied similar offices and posts in said incorporated subsidiaries.

7. Until on or about said May 17, 1957, plaintiff and his son together owned capital stock of AFR in amounts which varied from about 40% of all of its issued and outstanding capital stock to about 33% thereof, the latter being the amount thereof so owned from sometime in August, 1955 until on or about May 17, 1957.

8. On or about said May 17, 1957, plaintiff and his son sold to defendants other than Ackman<sup>and AFR</sup> all of the issued and outstanding stock of AFR held by them on that date and thereupon plaintiff resigned from employment by and all offices and all posts as director in AFR and its incorporated subsidiaries, except that he continued thereafter and until December 31, 1958 as consultant in matters relating to its business policy, to render services as such when called upon by AFR.

9. At all times herein mentioned until said May 17, 1957, defendants Alexander N. Fathy and de Montebello were with plaintiff all of the directors and principal executive officers of AFR and its incorporated subsidiaries and, at all said times after said date, defendants other than Ackman<sup>and AFR</sup> were such.



ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
AMERICAN FOAM RUBBER CORPORATION, BANKRUPT ("TRUSTEE"),  
AS AMENDED BY PRE-TRIAL ORDER

10. By virtue of the foregoing, plaintiff during all of the times herein mentioned until on or about May 17, 1957 had active charge of all of the operations and personnel of AFR, its subsidiaries and total organization and, at all times herein mentioned, plaintiff had an intensive, special and unique knowledge of and acquaintance with the business operations, affairs, transactions and assets of AFR and its subsidiaries and a close, special, unique and confidential relationship with all of the sales and other personnel employed by AFR and its subsidiaries, and was in a position and did to exercise substantial influence over all of the said personnel.

11. At or about the time of the sale by plaintiff and his son of their stockholdings and the former's almost complete retirement from the AFR organization, as aforementioned, plaintiff conceived, devised, entered upon and commenced to effect a willful, malicious, fraudulent and unlawful scheme, design and plan to destroy the ~~XXXXXX~~ business of AFR and its subsidiaries; force AFR into a condition of insolvency and bankruptcy, and acquire for himself all or substantially all of the tangible and intangible assets of AFR and its subsidiaries at a price and for a consideration amounting to only a small fraction of their actual worth.

ANSWER OF COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
AMERICAN FOAM RUBBER CORPORATION, BANKRUPT ("TRUSTEE"),  
AS AMENDED BY PRE-TRIAL ORDER

12. In pursuance of his said scheme, design and plan, plaintiff:

(a) explained and disclosed his scheme to AFR's key sales personnel, four persons who prior to May, 1957 had effected about 75% of the total sales to manufacturers using AFR products, and solicited and requested their joining, cooperating and participating with him in the operation and furtherance of said scheme by offering and promising to each of them a fractional share and interest in the tangible and intangible assets of AFR and its subsidiaries to be acquired under and pursuant to plaintiff's scheme and in all other unlawful benefits to be acquired by said scheme;

(b) offered and promised to each of the said personnel that he would, after acquiring control and ownership of the tangible and intangible assets of AFR and its subsidiaries, operate the same for a period of five years at a nominal salary and employ each of said personnel upon terms and conditions and at compensations substantially more generous and favorable than those under which they were then employed by AFR; and

(c) corruptly influenced three of said personnel, who prior to May, 1957 had effected about 60% of the total sales to manufacturers using AFR products, without



47a

ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
AMERICAN FOAM RUBBER CORPORATION, BANKRUPT ("TRUSTEE"),  
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the knowledge or consent of AFR or of its officers or directors, and solicited and requested them to join in a combination and conspiracy with him in furtherance of his scheme.

13. The mentioned three key sales personnel did, in fact, conspire and agree with plaintiff to and they did join with plaintiff in said combination and conspiracy and, in furtherance of both the scheme and conspiracy, plaintiff and said three jointly and severally did the following things, among others:

(a) substantially reduced the sales efforts of said three and deliberately held down to minimal amounts the sales made by them in their respective territories, and diverted substantial amounts of sales and business from AFR to its competitors;

(b) attempted to induce and procure the fourth of said key personnel by threats and corrupt inducements to similarly reduce his sales efforts in his sales territory and divert substantial amounts of sales and business from AFR to its competitors;

(c) obtained from other employees and from the files and records of AFR and its subsidiaries secret

ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
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and confidential information and data concerning its business, assets, liabilities and finances and disclosed the same to competitors of AFR;

(d) broadcast and spread among other employees of AFR and its subsidiaries false rumors of the imminent failure and collapse of the business of AFR and of its imminent insolvency and bankruptcy and persuaded the said other employees to terminate their employments with AFR and its subsidiaries;

(e) dissuaded prospective employees of AFR and its subsidiaries from entering into the employ of AFR and its subsidiaries;

(f) broadcast and spread destructive rumors and reports in the foam rubber industry and trade and elsewhere of the imminent collapse of the business of and insolvency and bankruptcy of AFR to impair its credit and bring it into disrepute with its customers and prospective customers; and

(g) effected on or about March 30, 1958 the resignations from the AFR organization of the mentioned three key sales personnel and the entering by them into employment in substantially the same sales capacities and territories



ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
 AMERICAN FOAM RUBBER CORPORATION, BANKRUPT ("TRUSTEE"),  
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with a competitor of AFR, the disclosure by them of secret and confidential trade information and data of AFR to said competitor and the commitment by them of assistance to each competitor in securing the business and customers of AFR.

14. By virtue of the foregoing, sales to manufacturers in the territories of said three key sales personnel were substantially reduced from and after May 17, 1957. AFR has been rendered insolvent and adjudged bankrupt and said AFR has sustained damage in the amount of \$2,000,000.

SECOND COUNTERCLAIM AGAINST PLAINTIFF AND  
 CROSS CLAIM AGAINST DEFENDANTS de MONTMOLLIN  
 AND ALEXANDER S. PATHY

15. Ackman repeats each of the allegations contained in paragraphs "3", "4", "6", "7", "8" and "9" as is here verbatim set forth.

16. At the time of the sale by plaintiff and his son of their stockholdings in AFR as aforementioned, on or about May 17, 1957, and as part of the said transaction, the parties herein, other than Ackman, <sup>AFR</sup> and Suzanne S. Pathy, caused AFR to and it did enter into an agreement in writing with plaintiff dated May 17, 1957 wherein and whereby AFR agreed to pay plaintiff the sum of \$100 at the time of the

ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
AMERICAN FOAM RUBBER CORPORATION, BANKRUPT ("TRUSTEE"),  
AS AMENDED BY PRE-TRIAL ORDER

making of the said agreement and \$25,700 in postponed installments, as at the time of the making of the said agreement, to cancel a debt owing by plaintiff to AFR in the amount of \$5,000 and at the time of the making of the said agreement to give to plaintiff property in the form of life insurance policies, having an aggregate cash value of \$14,234.

17. AFR thereupon and thereafter cancelled the mentioned debt, turned over to plaintiff the mentioned property and gave to plaintiff the mentioned cash of \$54,466. The debt cancellation, property turn over and payment of \$766 of said cash were made on or about May 17, 1957, \$27,500 of the balance of the cash was paid in three installments before the end of 1957 and \$26,200 of the said cash was paid in twelve installments before the end of 1958.

18. There was no consideration for said agreement or said cancellation of debt and turn over of property and cash and the same, in every part, constituted a conversion of the assets of AFR, an unjust enrichment of plaintiff at the expense of AFR and a betrayal of AFR by the parties herein, other than Ackman, AFR and Suzanne M. Pathy, who completely dominated and controlled AFR.

19. At all times mentioned in paragraphs "16" and "17" and since to date, persons, other than parties herein, held and hold claims against AFR which are provable under



ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
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the Bankruptcy Act and the transfers herein mentioned are,  
under state law applicable thereto, voidable for the reasons  
above stated by such creditors.

20. By virtue of the premises AFR and Ackman were  
damaged in the sum of \$73,700.

21. The action arises under subdivision "e" of  
§ 70 of the Bankruptcy Act, 11 U.S.C. 110, as hereinabove  
more fully appears.

WHEREFORE Ackman demands judgment

(b) against plaintiff on his first counter-  
claim in the sum of \$2,000,000 plus exemplary damage in the  
sum of \$1,000,000; and

(c) against all parties, other than Ackman,  
AFR and Suzanne M. Pathy, in the sum of \$73,700 with interest

ANSWER AND COUNTERCLAIM OF MILTON ACKMAN AS TRUSTEE OF  
AMERICAN FOAM RUBBER CORPORATION, BANKRUPT ("TRUSTEE"),  
AS AMENDED BY PRE-TRIAL ORDER

on \$20,000 from May 17, 1957, on \$27,500 from December 31,  
1957 and on \$25,200 from December 31, 1958;

together with the costs and disbursements of this action.

KLEEBERG & GREENWALD  
Attorneys for Defendant Ackman

By \_\_\_\_\_

Office & I. C. Address  
11 East 44th Street  
Borough of Manhattan (17)  
City of New York



## PLAINTIFF'S REPLY TO TRUSTEE'S COUNTERCLAIM.

UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK-----X  
SAMUEL BUCHMAN,

Plaintiff,

-against-

AMERICAN FOAM RUBBER CORPORATION,  
MARIE LOUISE de MONTMOLLIN,  
ALEXANDER F. PATHY and SUZANNE M.  
PATHY,Defendants.  
-----XCivil Action  
No. 60 Civ. 2328REPLYTO TRUSTEE'S ANSWER

Plaintiff, by his attorneys, Whyman and Neitlich,  
for his Reply to the Answer of defendant MILTON R. ACKMAN, as  
Trustee for American Foam Rubber Corporation, Bankrupt, alleges  
as follows:

IN REPLY TO SAID DEFENDANT'S  
FIRST COUNTERCLAIM

1. Denies each and every allegation set forth in  
paragraph "3" of the Trustee's Answer, except admits that on  
January 17, 1961 defendant AMERICAN FOAM RUBBER CORPORATION filed  
a Petition for an Arrangement under Chapter XI of the Bankruptcy  
Act, that on or about February 21, 1961 said corporation was  
adjudged a bankrupt, and that on or about February 23, 1961  
Milton R. Ackman was appointed Trustee in Bankruptcy of said  
corporation.

2. In reply to paragraph "5." of the Trustee's  
Answer: Plaintiff denies having knowledge or information

## PLAINTIFF'S REPLY TO TRUSTEE'S COUNTERCLAIM

sufficient to form a belief as to each and every allegation of said paragraph having reference to any events transpiring after May 17, 1957. Plaintiff denies each and every allegation of said paragraph "5." having reference to events transpiring prior to May 17, 1957, except admits that between the date of its incorporation and May 17, 1957, American Foam Rubber Corporation was engaged in the manufacture and sale of foam rubber pillows and cushions for industrial and consumer use, and conducted its operations through various departments or divisions; and plaintiff denies having knowledge or information sufficient to form a belief with respect to the so-called "incorporated subsidiaries" without further identification of said subsidiaries.

3. Denies each and every allegation set forth in paragraph "6." of the Trustee's Answer, except admits and alleges that plaintiff was one of the three organizers of American Foam Rubber Corporation in or about March, 1950, and that from the date of its incorporation until May 17, 1957, plaintiff was the president of said corporation, and one of its three directors, and was an officer of each of the corporate subsidiaries of American Foam Rubber Corporation.

4. Plaintiff admits each and every allegation set forth in paragraph "8." of Trustee's Answer, except that plaintiff



## PLAINTIFF'S REPLY TO TRUSTEE'S COUNTERCLAIM

refers to the actual written agreements of purchase and sale, and of employment, entered into May 17, 1957 between plaintiff and the several individual defendants and American Foam Rubber Corporation.

5. Denies each and every allegation set forth in paragraph 9 of Trustee's Answer with respect to the period until May 17, 1957, except that plaintiff admits that until May 17, 1957 plaintiff was an officer and director of American Foam Rubber Corporation, and its incorporated subsidiaries. Plaintiff denies having knowledge or information sufficient to form a belief with respect to the allegations of paragraph "9." of Trustee's Answer for the period after May 17, 1957.

6. Denies each and every allegation set forth in paragraph "10."

7. Denies each and every allegation set forth in paragraphs "11.", "12.", "13." and "14." of Trustee's Answer.

IN REPLY TO SAID DEFENDANT'S  
SECOND COUNTERCLAIM

8. With respect to paragraph "15." of the Trustee's Answer, plaintiff repeats each and every denial, admission and allegation hereinabove set forth with the same effect as if herein set forth in full with respect to the paragraphs referred to in paragraph "15." of the Trustee's Answer.

9. Denies each and every allegation set forth in paragraph "16." of Trustee's Answer with respect to the period

## PLAINTIFF'S REPLY TO TRUSTEE'S COUNTERCLAIM

up to and including May 17, 1957; and denies having knowledge or information sufficient to form a belief as to the allegations of said paragraph "16." for the period subsequent to May 17, 1957.

10. Denies having knowledge or information sufficient to form a belief as to each and every allegation set forth in paragraph "17." of the Trustee's Answer, except admits that on or about, and immediately prior to May 17, 1957 plaintiff owned and held 12,772 shares of the Class A Capital Stock of American Foam Rubber Corporation, and plaintiff's son, A. Sander Buchman, owned and held 5,550 shares of the Class A Capital Stock of said Corporation.

11. Denies each and every allegation set forth in paragraph "18." of Trustee's Answer, except admits that on or about April 1, 1950 American Foam Rubber Corporation authorized its Series A Debentures in the total amount of \$120,000.00, all of which debentures were issued and sold, and that on or about August 1, 1955 American Foam Rubber Corporation authorized its Series B Debentures in the total amount of \$300,000.00, of which \$223,000.00 were issued and sold; and plaintiff refers to the express written provisions of said debentures for the terms thereof.

12. Denies each and every allegation set forth in paragraphs "20." and "21." of Trustee's Answer.



## PLAINTIFF'S REPLY TO TRUSTEE'S COUNTERCLAIM

13. Denies each and every allegation set forth in paragraph 22 of Trustee's Answer, except admits that on or about May 17, 1957 plaintiff entered into an agreement with American Foam Rubber Corporation, and plaintiff refers to the express provisions of said agreement for the terms thereof.

14. Denies each and every allegation set forth in paragraph "23/" of Trustee's Answer, except admits that all payments required to be made by American Foam Rubber Corporation pursuant to its agreement of May 17, 1957 were made.

15. Denies each and every allegation set forth in paragraphs "24.", "25.", "26.", "27." and "28." of the Trustee's Answer.

AS AND FOR A FIRST COMPLETE  
DEFENSE TO SAID DEFENDANT'S  
COUNTERCLAIMS

16. The counterclaims alleged in the Trustee's Answer fail to set forth ~~claims~~ upon which relief can be granted.

AS AND FOR A SECOND COMPLETE  
DEFENSE TO SAID DEFENDANT'S  
COUNTERCLAIMS

17. The events alleged in the Trustee's counterclaims occurred more than three (3) years prior to the service and filing of the Trustee's Answer and are therefor barred by the applicable Statute of Limitations.

## PLAINTIFF'S REPLY TO TRUSTEE'S COUNTERCLAIM

WHEREFORE, plaintiff demands judgment dismissing the counterclaims set forth in the Trustee's Answer, and for judgment in favor of plaintiff and against the defendants herein as prayed for in the complaint, together with interest as provided by law, and with the costs and disbursements of this action as against all defendants.

WHYMAN and NEITLICH

By Murray Weitz  
a Member of said Firm  
Office & P.O. Address  
104 East 40th Street  
Borough of Manhattan  
City of New York



PLAINTIFF'S REPLY TO APPELLANTS' AMENDED AND SUPPLEMENTAL  
ANSWER.

UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK

-----X  
SAMUEL BUCHMAN,

Plaintiff

-against-

AMERICAN FOAM RUBBER CORPORATION,  
MILTON R. ACKMAN as Trustee of  
American Foam Rubber Corporation,  
Bankrupt, MARIE LOUISE de MONTMOLLIN,  
ALEXANDER F. PATHY and SUZANNE M.  
PATHY,

Defendants  
-----X

Civil Action  
No. 60 Civ. 2328

REPLY TO AMENDED  
AND SUPPLEMENTAL  
ANSWER OF INDIVIDUAL  
DEFENDANTS

Plaintiff, by his attorneys, WHYMAN and NEITLICH,  
for his Reply to the Amended and Supplemental Answer of defen-  
dants MARIE LOUISE de MONTMOLLIN, ALEXANDER F. PATHY and  
SUZANNE M. PATHY, alleges:

1. Denies each and every allegation of paragraph "6."  
of the Amended and Supplemental Answer, except admits and  
alleges that plaintiff was one of the three organizers of  
AMERICAN FOAM RUBBER CORPORATION, (hereinafter called AFR CORP.)  
and was president and a director thereof until May 17, 1957.  
Plaintiff denies knowledge or information with respect to the  
second sentence of paragraph "6." until further information  
is supplied as to the various "subsidiary corporations"  
referred to therein.

2. In reply to paragraph "7." of the Amended and  
Supplemental Answer: Plaintiff denies having knowledge or

PLAINTIFF'S REPLY TO APPELLANTS' AMENDED AND SUPPLEMENTAL  
ANSWER

information sufficient to form a belief as to each and every allegation of said paragraph having reference to any events transpiring after May 17, 1957. Plaintiff denies each and every allegation of said paragraph "7." having reference to events transpiring prior to May 17, 1957, except admits that between the date of its incorporation and May 17, 1957, American Foam Rubber Corporation was engaged in the manufacture and sale of foam rubber pillows and cushions for industrial and consumer use.

3. Denies each and every allegation of paragraph "8." of the Amended and Supplemental Answer, except admits that plaintiff was one of the three organizers of BURLINGTON HOLDING CORPORATION which, until May 17, 1957, was the owner of certain premises in Burlington, New Jersey, and which premises were leased to defendant AFR CORP; and plaintiff denies having knowledge or information sufficient to form a belief as to any events allegedly transpiring after May 17, 1957.

4. Denies each and every allegation of paragraph "9." of the Amended and Supplemental Answer except admits that on May 17, 1957, defendants ALEXANDER P. PATHY and MARIE LOUISE de MONTWOLLIN were directors and officers of AFR CORP., and that on or about May 17, 1957, approximately two-thirds of the common stock of AFR CORP. was owned by the said defendants, and approximately one-third was owned by plaintiff and his son, A. SANDER BUCHMAN.



PLAINTIFF'S REPLY TO APPELLANTS' AMENDED AND SUPPLEMENTAL  
ANSWER

5. Denies each and every allegation as set forth in paragraphs "10.", "11.", "12." and "13." of the Amended and Supplemental Answer.

6. Denies each and every allegation as set forth in paragraphs "14." and "15." of the Amended and Supplemental Answer, except admits that on or about May 17, 1957, plaintiff and his son, A. SANDER BUCHMAN, and the individual defendants herein entered into an agreement in writing providing for the sale by plaintiff and his son to said defendants of the shares of the capital stock of AFR CORP. and BURLINGTON HOLDING CORPORATION, then owned and held by said sellers, to the individual defendants; and plaintiff refers to the express written provisions of said agreement for the terms thereof.

7. Denies each and every allegation set forth in paragraph "16. (c)" of the Amended and Supplemental Answer.

8. Denies each and every allegation set forth in paragraphs "17.", "18." and "19." of the Amended and Supplemental Answer.

9. With respect to paragraph "20." of the Amended and Supplemental Answer, plaintiff repeats each and every denial and allegation hereinabove set forth with respect to paragraphs "6.", "7.", "8." and "9." of the Amended and Supplemental Answer.

PLAINTIFF'S REPLY TO APPELLANTS' AMENDED AND SUPPLEMENTAL  
ANSWER

10. Denies each and every allegation as set forth in paragraphs "21.", "22.", "23.", "24.", "25.", "26.", "27.", "28.", "29." and "30." of the Amended and Supplemental Answer.

AS AND FOR A FIRST COMPLETE  
DEFENSE TO THE COUNTERCLAIMS  
IN THE AMENDED AND SUPPLEMENTAL  
ANSWER

---

11. The counterclaims alleged in the Amended and Supplemental Answer fail to set forth claims upon which relief can be granted.

AS AND FOR A SECOND COMPLETE  
DEFENSE TO THE COUNTERCLAIMS  
IN THE AMENDED AND SUPPLEMENTAL  
ANSWER

---

12. The events alleged in the counterclaims occurred more than three (3) years prior to the service and filing of the Amended and Supplemental Answer and are therefore barred by the applicable Statute of Limitations.

WHEREFORE, plaintiff demands judgment against the individual defendants as prayed for in the complaint, and



PLAINTIFF'S REPLY TO APPELLANTS' AMENDED AND SUPPLEMENTAL  
ANSWER

dismissing the counterclaims set forth in the Amended and  
Supplemental Answer, together with the costs and disbursements  
of this action.

WHYMAN and NEITLICH  
Attorneys for Plaintiff

By Murray Weinstein  
a member of the firm  
Office & P.O. Address  
104 East 40th Street  
Borough of Manhattan  
City of New York (16)

APPELLANTS' REPLY TO TRUSTEE'S ANSWER.

UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK  
-----

SAMUEL BUCHMAN,

Plaintiff,

Civil Action  
No. 60 Civ. 2328

-against-

REPLY

AMERICAN FOAM RUBBER CORPORATION, MILTON  
R. ACKMAN, as Trustee of American Foam  
Rubber Corporation, Bankrupt, MARIE LOUISE  
de MONTMOLLIN, ALEXANDER F. PATHY and  
SUZANNE M. PATHY,

Defendants.  
-----X

Defendants MARIE LOUISE de MONTMOLLIN, ALEXANDER  
F. PATHY and SUZANNE M. PATHY, (hereinafter the replying  
defendants), by their attorneys, SELIGSON, MORRIS &  
NEUBURGER, replying to the Answer by the defendant, MILTON  
R. ACKMAN, as Trustee of defendant AMERICAN FOAM RUBBER  
CORPORATION, bankrupt(hereinafter the Trustee):

IN REPLY TO THE TRUSTEE'S CROSS CLAIM  
AGAINST THE ANSWERING DEFENDANTS:

1. Denies each and every allegation set forth in paragraph 20 of the Trustee's Answer.
2. Denies each and every allegation set forth in paragraph 22 of the Trustee's Answer except admits that on



## APPELLANTS' REPLY TO TRUSTEE'S ANSWER

or about May 17, 1957, American Foam Rubber Corporation entered into an agreement in writing dated May 17, 1957. The replying defendants beg leave to refer to the said agreement for a statement of the terms and conditions thereof.

3. Denies each and every allegation set forth in paragraph 23 of the Trustee's Answer except admits that all payments required to be made by American Foam Rubber Corporation, pursuant to the agreement of May 17, 1957, were made.

4. Denies each and every allegation set forth in paragraphs 24, 25, 26, 27 and 28 of the Trustee's Answer.

**AS AND FOR A FIRST AND COMPLETE AFFIRMATIVE  
DEFENSE TO THE TRUSTEE'S CROSS CLAIM AGAINST  
THE REPLYING DEFENDANTS:**

5. The Trustee's cross claim against the replying defendants fails to set forth a claim upon which relief can be granted.

**AS AND FOR A SECOND AND COMPLETE AFFIRMATIVE  
DEFENSE TO THE TRUSTEE'S CROSS CLAIM AGAINST  
THE REPLYING DEFENDANTS:**

6. The acts and transactions alleged in the Trustee's cross claim against the replying defendants occurred more

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## APPELLANTS' REPLY TO TRUSTEE'S ANSWER

than three years prior to the service and filing of the Trustee's Answer and are therefore barred by the applicable statute of limitations.

WHEREFORE, defendants MARIE LOUISE de MONTMOLIN, ALEXANDER F. PATHY and SUZANNE M. PATHY demand judgment dismissing the cross claim by the Trustee against them, together with the costs and disbursements.

Dated, New York, N. Y., March 17, 1962.

SELIGSON, MORRIS & NEUBURGER, ESQS.

By

Member of said firm, Attorneys  
for Defendants, Marie Louise de  
Montmollin, Alexander F. Pathy  
and Suzanne M. Pathy  
Office & P. O. Address  
350 Fifth Avenue  
New York 1, New York



OPINION OF HON. IRVING BEN COOPER, U.S.D.J., AUGUST 17,  
1966, #32646, DENYING PLAINTIFFS' MOTION FOR  
SUMMARY JUDGMENT.

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

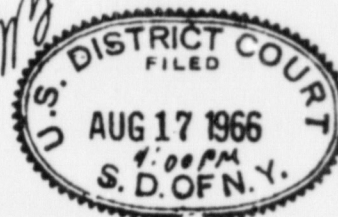
FIRST NATIONAL BANK OF HOLLYWOOD,  
DOROTHY BUCHMAN and A. SANKER BUCHMAN,  
as Executors of SAMUEL BUCHMAN,  
Deceased,

Plaintiffs,

-against-

AMERICAN FOAM RUBBER CORPORATION,  
MILTON R. ACKMAN, as Trustee of  
AMERICAN FOAM RUBBER CORPORATION,  
MARIE LOUISE de MONTMOLLIN,  
ALEXANDER F. PATHY and SUZANNE M.  
PATHY,

Defendants.



# 32646

60 Civ. 2328

MEMORANDUM



IRVING BEN COOPER, D.J.

This is a motion under Rule 56, F.R.Civ.P. seeking  
judgment in behalf of plaintiffs<sup>1</sup> on the first counterclaim  
interposed in the amended and supplementary answer filed by

1. By order dated December 2, 1965, executors of Samuel Buchman were substituted as parties plaintiff. Samuel Buchman, the original plaintiff, died in November, 1965.

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the individual defendants.<sup>2</sup> See Rule 12(c), F.R.Civ.P.

In essence, plaintiffs maintain that the individual defendants' first counterclaim sets forth, at most, a cause of action cognizable only in the right of American Foam Rubber Corporation (hereinafter AFR) and does not state a claim upon which relief can be granted to them individually as stockholders in the now bankrupt corporation. By memoranda and affidavits,<sup>3</sup> the individual defendants take the contrary view and assert that there are triable issues of fact which preclude granting the motion. We agree.

2. This action has been assigned under Rule 2 of the local rules. The background of the proceedings is set forth in this Court's opinion on prior motions for summary judgment directed at the second counterclaim filed by the Trustee of American Foam Rubber Corporation. See 250 F.Supp. 60 (S.D.N.Y. 1965). The Trustee has submitted no papers on the instant motion.

3. The Court has not considered, in ruling upon the motion, papers untimely filed except to the extent they are deemed "corrections" of papers theretofore submitted. See letter of Martin N. Whyman, Esq., dated June 19, 1966, addressed to the Court and filed herewith.



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Under New York law, upon which the parties rely, it is agreed between them that interference with a corporation's business or waste and mismanagement of its assets, is generally considered a wrong to the corporation alone, subject to redress only through an action by or in the name of the corporation. In such a situation, individual stockholders, although injured indirectly by depreciation of the value of stock held, or loss of future dividends etc., have no independent cause of action in their own behalf. Hiles v. New York Central and Hudson River R.R., 176 N.Y. 119 (1903); see Gordon v. Elliman, 306 N.Y. 456, 466 (1954); Green v. Victor Talking Machine Co., 24 F.2d 338 (2d Cir. 1928), cert. denied 278 U.S. 603.

There are, however, a series of cases recognizing that certain conduct constituting wrongs to the corporation also constitute direct injury to individual stockholders upon which individual suit may be brought. See cases cited in Coronado Development Corp. v. Millikin, 175 Misc. 1, 32 N.Y.S.2d 670, 673, 675 (N.Y. Co., 1940) appeal dismissed, 362 N.Y.S.2d 1019, 30 N.Y.S.2d 847 (1941). As noted in Hiles (176 N.Y. 123-4):

There are wrongs which, if committed against a stockholder entitle him to a right of action against the

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person committing the wrong for the damages sustained, as, for instance, where a person had been induced to purchase stock in a corporation and pay a higher price than the stock was fairly and reasonably worth, or where the owner of stock had been induced to part with it for a less sum than its true value, by reason of false and fraudulent representations of others with reference to its value. Rothmiller v. Stein, 143 N.Y. 581, 27 L.R.A. 148, Ritchie v. McMillen, 79 Fed. 522. But these wrongs are distinguishable from those against the corporation. They result in injury to the stockholder upon whom the wrong is practiced, but do not injure the other stockholders or the corporation itself.

Further, where "wrongful acts are not only wrongs against the corporation, but are also violations by the wrongdoer of a duty arising from contract or otherwise, and owing directly by him to the stockholders," New York courts have permitted direct suit by individual stockholders. General Rubber Co. v. Benedict, 215 N.Y. 18 (1915). See Von Au v. Magenheimer, 126 A.D. 257 (1908), aff'd, 196 N.Y. 510 (1909); In re Auditors' Will, 249 N.Y. 335 (1928); Breitel, J. dissenting in Greenfield v. Penner, 6 A.D.2d 263, 175 N.Y.S.2d 919, 921 (1st Dept. 1958) (decision of Appellate Division reversed "for the reasons [therein] set forth" 6 N.Y.2d 867 (1959)); Coronado Development Corp. v. Millikin, *supra*; cf. Amendola v. Lianides, 15 Misc.2d 80, 181 N.Y.S.2d 89 (Kings 1958) (dismissing complaint with leave to replead) (amended complaint



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upheld on motion to dismiss, see 8 A.D.2d 735, 187 N.Y.S.2d  
267 (2d Dept. 1959)).

The issue, therefore, is whether the amended and  
supplementary answer's first counterclaim sets forth a cause  
of action which, under New York law, may be asserted by  
stockholders individually, and if so, whether in regard there-  
to triable fact issues exist.

Individual defendants' first counterclaim is set  
forth in paragraphs 6 to 19 of the amended answer and makes  
detailed allegations covering eight pages. Briefly, it  
alleges that between mid-1955 and May 17, 1957, Samuel Buchman  
and his son owned 33 1/3% of AFR's common stock, the remainder  
being owned by the individual defendants (§9(e)); that on or  
about May 17, 1957, Buchman and his son agreed in writing to  
sell to individual defendants all their capital stock in AFR  
and an affiliated company (§14); that under the agreement,  
Buchman was to and did resign forthwith (§15(c), 16(d));  
that individual defendants deposited with Buchman's attorney,  
in escrow, all shares of stock purchased, against payment of  
promissory notes made under the agreement, the amount thereof  
being thereafter paid (§16(a)-(b)).

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Further, on information and belief, on or about May 17, 1957, and simultaneously with the making and execution of the agreement discussed above, "Buchman conceived, devised, entered upon and commenced to effect a willful, malicious, fraudulent and unlawful scheme, design and plan [redacted] to destroy AFR's business; force it into insolvency and bankruptcy; render valueless the stock sold to individual defendants under the May 17, 1957 agreement and acquire for himself all assets of AFR and affiliated companies at a small fraction of their actual worth but for his conduct. (¶17)

Similarly, the means by which the scheme was to be effected (¶17) and indeed the success thereof (¶18) are alleged in part as follows: Buchman induced three of the four key sales personnel to join with him by offering them a fractional share interest in AFR assets to be acquired under the scheme; when successful, they would operate AFR for five years with more generous compensations than they presently earned; the sales personnel deliberately held down sales and diverted business to AFR competitors; disclosed to competitors business and financial information of a secret and confidential nature; spread false rumors of AFR's imminent collapse, persuading other employees



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to resign; dissuaded prospective employees from entering AFR's employ; themselves, resigned in March, 1958, entering employment in substantially the same sales capacities and territories with a competitor of AFR, disclosing trade secrets, which conduct has continued at various times since March 30, 1958.

As a result, it is alleged (¶19) that AFR sales in the territories of these personnel were reduced from \$2.3 million<sup>4</sup> in 1957 to \$1.1 million in 1958 and to \$703 thousand in 1959; AFR was rendered insolvent and adjudicated bankrupt; the stock purchased under the May 17, 1957 agreement has been rendered valueless; debentures held by individual defendants issued by AFR and affiliates have been rendered valueless; past and future compensations and profits have been lost by individual defendants; and their business reputations and standing have been seriously impaired.

At the foot of their Second Counterclaim, the individual defendants demand judgment on their counterclaim against plaintiffs in the amount of \$2,000,000, together

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4. Amounts rounded.

5. This counterclaim (essentially alleging an action for fraud and deceit upon facts almost identical to those alleged on the first counterclaim) is not involved in this motion. The prayer for relief does not distinguish between the counterclaims.

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with exemplary damages in the amount of \$1,000,000 with costs and disbursements of the action.

Plaintiffs' reply denies the material allegations and asserts as a complete defense that the facts set forth fail to state a claim upon which relief can be granted.

Plaintiffs take the view that this pleading sets forth no basis for a finding that Buchman did the alleged acts with intent to directly injure the individual defendants, or breached any duty owed to them, arising from contract or otherwise; rather, being almost identical to the Trustee's first counterclaim in behalf of the bankrupt AFR, it merely alleges wrongs directly injuring the corporation for which individual stockholders have no personal cause of action. See, e.g. Plaintiffs' Reply Memorandum, p.10.

Individual defendants' memorandum contends, however, that the complaint sets forth mediate facts from which, taken alone and with the affidavits submitted on this motion, show that Buchman, by contract and through his close personal relationship with them, owed them a duty of acting in good faith and not to destroy the value of the property sold to them. Thus,



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they argue that the sale agreement of May 17, 1957 was "instinct with obligation" and contained by law an implied covenant that neither party would destroy the right of the other party to the fruits of the contract (Individual Defendants Memorandum, p. 20), see Kirke LaShelle Co. v. Paul Armstrong Co., 263 N.Y. 79, 87 (1933); that under the escrow agreement by which Buchman's attorney held shares of stock pending final payment of the purchase price, due January 2, 1959, their relationship to him was that of pledger and pledgee, see Kono v. Roeth, 237 A.D. 252, 260 N.Y.S. 662 (1st Dept. 1932); in any event, despite some personality and policy differences regarding the business, Buchman and individual defendants, all the stockholders, officers and directors of APR, a close corporation, had worked together for several years, had reason to and did repose trust in each other and thus the circumstances surrounding the negotiation of the May 17, 1957 agreement was not at arms length (Individual Defendants Memorandum, pp. 30-31). No case is cited in support of this final claimed basis of finding, between Buchman and the individual defendants, the privity existing in such cases as General Rubber Co. v. Benedict, supra

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(corporation v. director); Von Au v. Magenhaimer, supra  
(plaintiff executor v. shareholders who fraudulently caused  
sale of stock owned by testator); In Re Auditor's Will,  
supra (surety held liable for directors misappropriation of  
corporate funds where corporation's judgment uncollectible  
against his estate). Moreover, under the Severance Agreement,  
Buchman obligated himself to remain available to give advice  
to AFR on a consulting basis until December, 1953 (See Affi-  
davit of David Sive, Esq., sworn to May 20, 1966, ¶12).

Plaintiffs rejoin that:

All of the theories ... above, are support-  
ed in and of themselves, and might conceivably  
be the basis of a personal cause of action in be-  
half of the individual defendants, but the alle-  
gations contained in the first counterclaim ...  
are not framed on the basis of any one of said  
theories. The theory of the first counterclaim  
is a conspiracy to damage the business and affairs  
of AFR.

(Plaintiffs' Reply Memorandum, p. 12)

We agree that the "framing" leaves much to be desired if the  
particular nuances of duty and obligation now expressly re-  
laid on by individual defendants were to be made plain and  
concrete, furnishing adequate notice, as a matter of original  
pleading.



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1966, #32646, DENYING PLAINTIFFS' MOTION FOR  
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However, as Judge Metzner expressly noted in his decision granting individual defendants leave to file the counterclaim (decision of December 7, 1961), the issues posed by it were already before the court in the trustees pleading. Although his decision did not expressly rule on sufficiency, there is no claim now that the details and underlying facts supplied by affidavit came as a surprise to plaintiffs or subject plaintiffs to any prejudice. Nor can we find any reason for treating the pleading as insufficiently incorporating the terms of the May 17, 1957 agreements. F.R.Civ.P., Rules 8(e), (f). Cf. 2 Hornstein, Corporation Law and Practice §716, p.206; p. 98, n.8F (1966 Supp).

As to plaintiffs' view of the legal theory on which they contend the complaint was "framed," it is sufficient at this stage to note that the inadequacies are not fatal. No pre-trial order has been entered. Even where such has been entered, it can be modified "to prevent manifest injustice." Scott v. Spanier Bros., 298 F.2d 928 (2 Cir. 1962). At trial, moreover, pleadings can be deemed amended to conform to the proof. F.R.Civ.P., Rule 15(b). Finally, plaintiffs themselves realize that among the cases relied on by individual defendants, in support of their 15(a) motion to add the counterclaim,

OPINION OF HON. IRVING BEN COOPER, U.S.D.J., AUGUST 17,  
1966, #32646, DENYING PLAINTIFFS' MOTION FOR  
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is General Rubber Co. v. Benedict, supra, expressly reasserted in opposition here. See Plaintiffs' Memorandum, p.13. No claim of prejudice or surprise thereto is made. See Plaintiffs' Reply Memorandum, p.8.

With a view to narrowing issues in aid of preparation of a pre-trial order, it might have been possible to rule upon the express theories relied upon in light of any uncontroverted material facts. However, since the memoranda of the parties clearly show there is much conflict concerning the meaning and legal effect of the May 17, 1957 agreements and the interpretations to be accorded the circumstances in which they were entered, this we decline to do. See Miller v. General Outdoor Advertising Co., 337 F.2d 944 (2d Cir. 1964); Union Ind. Soc. of Canton, Ltd. v. William Gluckin & Co., Inc., 333 F.2d 946 (2d Cir. 1965). In proposing the terms of the pre-trial order, the parties should consider such modifications in the individual defendants' first counterclaim as reflect the positions asserted in the papers submitted herein.

Plaintiffs' motion for summary judgment under Rule 56, F.R.Civ.P. is denied.

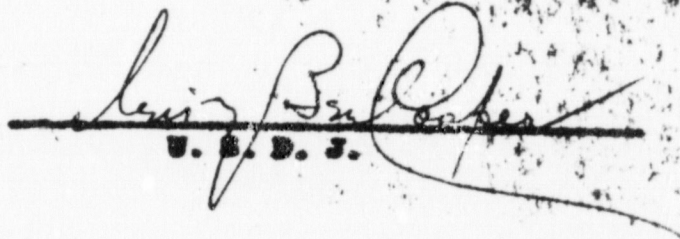


OPINION OF HON. IRVING BEN COOPER, U.S.D.J., AUGUST 17,  
1966, #32646, DENYING PLAINTIFFS' MOTION FOR  
SUMMARY JUDGMENT

This shall be considered an order; settlement  
thereof is unnecessary.

SO ORDERED:

New York, N.Y.  
August 17, 1966

  
U. S. D. J.

OPINION OF HON. IRVING BEN COOPER, U.S.D.J., MAY 9, 1967,  
#33489 DENYING APPELLANTS' MOTION FOR SUMMARY JUDGMENT.

UNITED STATES DISTRICT COURT,  
SOUTHERN DISTRICT OF NEW YORK.

-----X

FIRST NATIONAL BANK OF HOLLYWOOD, DOROTHY BUCHMAN and A.  
SANDER BUCHMAN, as Executors of SAMUEL BUCHMAN, Deceased,

*Plaintiffs,*

*-against-*

AMERICAN FOAM RUBBER CORPORATION, MILTON R. ACKMAN,  
as Trustee of AMERICAN FOAM RUBBER CORPORATION,  
MARIE LOUISE de MONTMOLLIN, ALEXANDER F. PATHY  
and SUZANNE M. PATHY,

*Defendants.*

-----X

IRVING BEN COOPER, D. J.

In 1957 plaintiffs' decedent, Samuel Buchman, sold his capital stock in American Foam Rubber Corporation. As part of that transaction an agreement was reached whereby the individual defendants consented to the subordination of their debentures to those held by Buchman.

In 1958 defendants exchanged their debentures for preferred stock of American Foam Rubber Corporation. In their complaint plaintiffs allege that this exchange violated the prohibition in the subordination agreement against any payment by American Foam Rubber on defendants' debentures unless Buchman's debentures were first paid in full.



OPINION OF HON. IRVING BEN COOPER, U.S.D.J., MAY 9, 1967,  
#33489 DENYING APPELLANTS' MOTION FOR SUMMARY JUDGMENT

Defendants now move for summary judgment, asserting that there are no further facts to be adduced. We disagree.

The plain meaning of the subordination agreement is to prohibit defendants from realizing any cash or its equivalent from the corporation on their debentures until Buchman's debentures had been satisfied in full. Under certain clear and unmistakable circumstances the exchange of debentures for preferred would not violate the subordination agreement.

It might well be argued, however, that such an exchange could very well be a first step in a plan to obtain cash -- or cash realizable property -- from the corporation. Defendants' papers do not negate this possibility. Until such possibility is excluded, we regard it the better course to await the presentation of evidence at trial. To decide this question of fact by summary procedure is hazardous.

The individual defendants and the trustee in bankruptcy move in the alternative to sever plaintiffs' causes of action from the defendants' counterclaim. At this point in these proceedings the record does not indicate that the advantages claimed by defendants outweigh the value of having the jury grasp all implications

OPINION OF HON. IRVING BEN COOPER, U.S.D.J., MAY 9, 1967,  
#33489 DENYING APPELLANTS' MOTION FOR SUMMARY JUDGMENT

of the involved and seemingly bitter transactions that  
are the source of this litigation.

Defendants motion is denied without prejudice to  
renew.

This shall be considered an order; settlement  
thereof is unnecessary.

SO ORDERED!

New York, N. Y.  
May 9, 1967

IRVING BEN COOPER  
UNITED STATES DISTRICT JUDGE



20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36 X

Defendants. :

# AFFIDAVIT

STATE OF NEW YORK )  
 ) SS.:  
COUNTY OF NEW YORK )

ALEXANDER F. PATHY, being duly sworn, deposes  
and says:

1. I am one of the INDIVIDUAL DEFENDANTS herein. I make this affidavit in support of the INDIVIDUAL DEFENDANTS' renewed motion for summary judgment, dismissing the second cause of action of the complaint herein (hereinafter

AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

in this and accompanying papers sometimes referred to as the "Pleading"). I am fully familiar with the matters hereinafter related.

2. As is indicated in the annexed affidavit of DAVID SIVE, Esq., BUCHMAN claims that the subordination provisions (hereinafter in this and accompanying papers sometimes referred to as the "Subordination Agreement") of the Buy-Sell Agreement were violated by the Exchange.

3. This Court, in denying, without prejudice to renew, the INDIVIDUAL DEFENDANTS' earlier motion, has ruled that the one question raised by the Pleading is that of whether the Exchange was "a first step in a plan to obtain cash - or cash realizable property - from the corporation." This Court held that the papers before it on the earlier motion did "not negate [that] possibility." I verily believe that this affidavit and the accompanying papers now negate that possibility.

4. The facts are that the Exchange was intended to serve and did serve a purpose precisely opposite to that



AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

of obtaining cash or cash realizable property from the Company. Its purpose and effect - as well as that of a number of other measures taken by the INDIVIDUAL DEFENDANTS between May 1957 and December 1960 - were to strengthen the financial condition and standing of the Company, by substantially increasing its capital and sharply bettering its credit rating. To have used the Exchange, as a "first step" or otherwise, in a "plan to obtain cash - or cash realizable property - from the corporation", if it could have been done, would not only have defeated that purpose, but would have gravely injured and prejudiced the Company. There was never any thought of so using the Exchange. It could not have been so used. It was not so used.

5. The facts will demonstrate that:

A. The purpose and effect of the Exchange, as well as of a simultaneous donation to the Company by the INDIVIDUAL DEFENDANTS of substantial assets, was as stated above.

B. The Exchange and simultaneous donation of assets substantially increased the borrowing capacity of the Company with a principal source of outside financing,

AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

The Pennsylvania Company For Banking And Trusts (hereinafter in this and accompanying papers referred to as the "Pennsylvania Bank" or the "Bank").

C. The Exchange and the simultaneous donation of assets secured for the Company, for the first time, high credit ratings from Dun & Bradstreet, Inc. and the National Credit Office.

D. The Exchange seriously disadvantaged the INDIVIDUAL DEFENDANTS with respect to obtaining "cash - or cash realizable property - from the corporation."

E. Under the agreement between the Company and the Pennsylvania Bank, governing until December 1959, the INDIVIDUAL DEFENDANTS and the Company were unable to use the Exchange as a means of obtaining cash or cash realizable property from the Company.

F. Under the agreements with Walter E. Heller & Co., Inc., which succeeded the Pennsylvania Bank as a source of financing, the same disability continued, until the bankruptcy of the Company.

G. After the Exchange the INDIVIDUAL DEFENDANTS never used or even considered using the Exchange as a "first step in a plan to obtain cash - or cash realizable



AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

property - from the corporation"; every aspect of the Exchange and related further action was to serve and did serve a directly contrary purpose.

- A. The purpose of the Exchange was to strengthen the financial condition and standing of the Company by substantially increasing its capital and sharply bettering its credit rating.

6. The Exchange was a fundamental part of a plan and program of the Company management, the INDIVIDUAL DEFENDANTS, to strengthen the financial position and substantially better the credit standing and rating of the Company. This plan and program was undertaken and begun to be put into operation shortly after the Buy-Sell Agreement. As I pointed out in my earlier affidavit in support of the prior summary judgment motion, "during the entire history of the Company, from its organization in 1950, it had suffered from insufficient capitalization", the "Company's main competitors, at all times, [being] the large corporations in the United States manufacturing rubber and foam rubber products." (p. 21).

7. In early 1958, the increase of the capital of the Company was a matter of importance. 1957 was the

AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

first full year of business of the Company's Industrial Division, organized and activated in late 1956. Total sales increased from \$3,722,423 in 1956 to \$7,001,232 in 1957. With the commencement of the operations of the Industrial Division in late 1956 the Company had begun factoring its accounts receivable with Hubshman & Co. Inc.

8. In the latter part of 1957 it was determined by the Company management, the INDIVIDUAL DEFENDANTS, that the capital of the Company be increased to over \$1,000,000 in order to: a) increase its capacity to borrow from a principal source of its outside financing, the Pennsylvania Bank; and b) secure a high credit rating from two principal credit rating agencies, Dun & Bradstreet, Inc. and the National Credit Office.

It was anticipated that some increase of capital would result from retaining earnings (earned surplus) but that additional measures would be necessary to achieve the million-plus figure. Two measures were decided upon to achieve this: a) to convert \$300,000 of long-term debt into capital, and b) to contribute to capital an additional \$120,000, by contribution by the INDIVIDUAL DEFEND-



AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

ANTE to the Company of the shares of stock of Burlington Holding Corporation (hereinafter in this and accompanying papers referred to as "Burlington") owned by them individually. The INDIVIDUAL DEFENDANTS at that time owned 90 shares, constituting all of the issued and outstanding shares of the capital stock of Burlington. Thirty of the said 90 shares had been purchased by the INDIVIDUAL DEFENDANTS from BUCHMAN under the Buy-Sell Agreement, for the aggregate price of \$40,000.

9. The Exchange was a transaction converting debt into equity, the nature and effect of which are clear from financial statements of the Company. I annex hereto, as Exhibit A, a copy of a statement of liabilities and capital of the Company as at February 2, 1958, shortly before the Exchange. The statement was prepared by Edward Isaacs & Company, accountants for the Company, during the entire period of the transactions involved in this action. I respectfully direct this Court's attention to the "Liabilities and Capital" page of the statement, and, more particularly, to the portions thereof setting forth the Company's "Long-

## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

Term Debt" and its "Capital". The Long-Term Debt of the Company, totalling \$673,000, consisted then of three items of indebtedness, to wit:

5% Debenture Bonds Payable	\$273,000
Mortgage Notes Payable	
Plant and Equipment	175,000
Notes Payable	
Stockholders	100,000
Other	<u>25,000</u>
	\$673,000

10. Of the 5% Debenture Bonds, aggregating \$373,000 in principal amount, \$112,000, including the \$64,000 which are the subject of the Complaint, were bonds held by BUCHMAN. The balance were held by Mrs. de MONTMOLLIN.

11. The second item of the Long-Term Debt was mortgage notes payable on the Company's plant and equipment. The payee of those notes was the Pennsylvania Bank, which had entered into an agreement with the Company to assist in financing the organization of the Industrial Division (hereinafter in this and accompanying papers sometimes referred to as the "Term Loan Agreement"), a copy of which is annexed hereto as Exhibit "E". Under the said agreement, the Pennsylvania Bank agreed to lend to the Company, "from time to time amounts not exceeding in the ag-



AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

gregate \$400,000." (Section 2), secured by real property and chattel mortgages. The loans were to be evidenced by temporary notes, and by a "Permanent Note", when the full \$400,000 was lent. The principal of the Permanent Note was payable in sixteen equal quarter-annual installments.

12. The third item of the Long-Term Debt referred to in the February 2, 1958 statement consisted of "Notes Payable, stockholders and other." Those to stockholders aggregated \$100,000, all of which were payable to Mrs. de MONTMOLLIN. The "other" was BUCHMAN, who, as described in the Buy-Sell Agreement (Paragraph "Sixth B"), was "the holder of a five (5%) percent promissory Note of American Foam in the sum of \$25,000." Under paragraph "B" of the Subordination Agreement the notes held by Mrs. de MONTMOLLIN were subordinated to the Note held by BUCHMAN.

13. The "Capital" of the Company, as set forth on the February 2, 1958 statement, consisted of "capital stock" and "surplus". The capital stock aggregated \$287,330. The "surplus", all of which was earned surplus, was \$365,144. There was no capital surplus. The capital aggregated \$652,474.

## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

14. What was the effect of the Exchange upon the accounts of the Company? To answer that question, I turn to another financial statement of the Company, one dated April 30, 1958, setting forth the results of an examination of the Company's accounts by the same accountants, for the period of January 1 to March 30, 1958, together with a statement of the financial condition of the Company as at March 30, 1958. A copy thereof is annexed as Exhibit "C". The Exchange actually took place after March 30, 1958, but the statement as of March 30, 1958 is the earliest, as far as I can recall, giving effect to the Exchange, the statement setting forth the following note:

Note: This statement gives effect to conversion of Long-Term Debt to preferred stock, and the acquisition of the stock of Burlington Holding Corp. by donation of their stockholdings. Both transactions were completed after March 30, 1958."

The "conversion" referred to was the Exchange. The details of the donation of Burlington stock are herein-after described in this affidavit.

15. I respectfully direct this Court's attention to the statement, reproduced below, of the "Long-Term Debt" and the "Capital" of the Company, as set forth in the March



## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

30, 1958 statement. To aid this Court in understanding the effect of the Exchange, I star (\*) each amount affected by the Exchange, as well as by the simultaneous donation of the shares of the capital stock of Burlington, and follow each such amount with a legend, set forth in parentheses, describing the effect of the Exchange thereon:

Long Term Debt

5% Debenture Bonds Payable	\$142,000*	(reduced from \$373,000)
Mortgage Notes Payable - Plant and Equipment	175,000	
Notes Payable:		
Stockholders	31,000*	(reduced from \$100,000)
Other	<u>25,000</u>	
<u>Total Long-Term Debt</u>	\$373,000*	(reduced from \$673,000)

Capital

Capital Stock Issued -		
Preferred	\$300,000*	(a new item)
Common	278,330	
Capital Surplus	120,000*	(a new item, created by the donation of Burlington shares)
Earned Surplus:		
Balance-January 1, 1958	\$291,305	
Add: Net Profit for the Period	<u>31,613</u>	
Balance - March 30, 1958	<u>322,918</u>	
<u>Capital</u> - March 30, 1958	\$1,021,248*	(increased by \$420,000)

## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

16. Stated otherwise, in and by the Exchange and the donation of Burlington shares:

- a. the principal amount of debentures outstanding was reduced from \$373,000 to \$142,000;
- b. the principal amount of notes payable to stockholders (the INDIVIDUAL DEFENDANTS) was reduced from \$100,000 to \$31,000;
- c. the total "Long-Term Debt" of the Company was reduced from \$673,000 to \$373,000;
- d. the capital of the Company was increased by \$300,000 (the sum of the amounts by which debentures outstanding and notes to stockholders were reduced) by the addition to Capital Stock Issued of 3,000 shares of preferred stock, of a par value of \$100.00 each, in the aggregate amount of \$300,000;
- e. the assets were increased by the addition of the amount of the value of the Burlington shares, \$120,000, by which amount the capital was also increased.

17. The certificates for the 3,000 shares of preferred stock issued pursuant to the Exchange, which were actually executed and delivered on or about May 27, 1953 to Mrs. de MONIMOLLIN and her children, bore the following numbers and were in the following amounts of shares:



## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

<u>Cert. No.</u>	<u>No. Shares</u>
P1	2,000
P2	900
P3	10
P4	45
P6	45

In consideration of the issuance to her of the said certificates of stock, aggregating 3,000 shares, Mrs. de MONTMOLLIN surrendered for cancellation (a) debentures owned by her in the aggregate principal amount of \$231,000, and (b) notes owned by her in the aggregate principal amount of \$69,000.

13. The formal corporate action to increase the capital of the Company, by the Exchange, was taken in April and May 1958, after a series of informal discussions and meetings. At a special meeting of the Board of Directors held on April 10, 1958, at which there were present Mrs. PATHY and Mrs. de MONTMOLLIN and myself, I reported (quoting from the minutes) "on the advisability of increasing the capital of the Corporation to one million dollars (\$1,000,000.00 by authorizing 60,000 additional shares of Class A stock and 3,500 shares of 5% cumulative preferred stock of the par value

AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

of \$100 each. [I] submitted a form of certificate of amendment to the certificate of incorporation and explained the provisions thereof relating to the preferred stock."

The "provisions thereof relating to the preferred stock", explained by me, included the provisions hereinafter discussed relating to the rights to dividends and redemption, and a comparison of those rights with the rights of holders of the debentures to be exchanged. I then (quoting again from the minutes) "stated that upon approval of the proposed amendment by the stockholders it would be possible to convert part of the presently outstanding debt of the Corporation to stockholders to preferred stock ... [I] explained the advantages resulting therefrom to the Corporation by improving its credit and strengthening its capital structure." The following resolution was then adopted:

"RESOLVED, that the form of certificate of amendment of certificate of incorporation submitted to the meeting be, and it hereby is, approved, and that the proper officers of the Corporation be, and they hereby are, authorized and directed subject to approval of the proposed amendment by the stockholders of the Corporation, to execute, acknowledge and file a certificate of amendment of certificate of incorporation substantially in the form submitted to the meeting and to execute such further document or documents in the name and in behalf of the Corporation, under its corporate seal or otherwise,



## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

and to take any and all other action as they shall deem necessary or appropriate to carry out the proposed amendment of the certificate of incorporation of the Corporation; and

RESOLVED, that a meeting of the stockholders for the purpose of considering and acting on the proposed amendment be called for such date, time and place as the President shall deem appropriate."

19. On the following day, a special meeting of the stockholders of the Company was held. Present were the holders of all issued and outstanding shares of stock. A copy of the minutes of that meeting, including the necessary stockholders' resolution is annexed hereto as Exhibit "D". The further corporate action to authorize the actual exchange was described by me in my earlier affidavit, paragraph 25 of which I restate here:

"25. Thereafter and on or about April 17, 1958, a Certificate of Amendment of the Certificate of Incorporation of the Company was filed with the Secretary of State of the State of New York, providing for the increase of capital, by the authorization of additional shares of Class A common stock and creation of a new class of 5% Cumulative Preferred stock. This action was reported to a special meeting of the Board of Directors of the Company held on April 23, 1958. At the meeting of April 23, 1958, it was resolved that shares of the new 5% Cumulative Preferred stock be issued in exchange for Series A and Series B debentures of the corporation, at the rate of one share of stock for each \$100 face amount of said debentures. ..."

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20. At or about the same time that the Exchange was effected, the second aspect of the plan to increase the capital was carried out. Ninety shares, constituting all of the shares of the capital stock of Burlington issued and outstanding, were transferred by my wife, Mrs. de MONTMOLLIN and myself to the Company. Nothing was received by any of us; the shares were donated. The value of the shares -- the amount added thereby to the assets and to the capital of the Company as "capital surplus" -- was fixed at \$120,000, by reference to the price of \$40,000, fixed for BUCHMAN's 30 shares (one-third) of Burlington, in and by the Buy-Sell Agreement.

21. The Exchange and donation were simple and straightforward transactions. Their purpose was to increase the capital to over \$1,000,000 and to thereby strengthen the financial condition and standing of the Company. Dramatic proof of the effect lies in the actions taken at the time of and in direct response to the Exchange and donation of Burlington shares, by the important financial and credit rating institutions with which the Company then dealt.



AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

- B. The Exchange and simultaneous donation of assets substantially increased the borrowing capacity of the Company with the Pennsylvania Bank.

22. I have heretofore referred to the Term Loan Agreement. In 1958, the Pennsylvania Bank was, as it had been for several years theretofore and as it continued to be until December 1959, a principal source of outside financing for the Company. The financing by the Pennsylvania Bank took two forms: a) a term loan evidenced by the "Permanent Note" and secured as described in paragraph "11" above; and b) an unsecured revolving loan or loans, evidenced by a note or notes. The term loan was governed by the Term Loan Agreement, a copy of which is annexed hereto as Exhibit B. The unsecured loans were not provided for in any underlying agreement. They were evidenced by short term notes.

23. At the end of 1957 the Company was indebted to the Pennsylvania Bank in the principal amount of \$320,000 under the Term Loan Agreement. Up to that time the maximum amount of unsecured credit extended had been \$100,000. This short term unsecured indebtedness of \$100,000 had been borrowed earlier in 1957. The Company, however, needed additional financing, as indicated above, part of which was

AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

to be supplied by the INDIVIDUAL DEFENDANTS, by the two steps described in paragraph "8" above. Part was to be sought from the Pennsylvania Bank, in and by resumption and enlargement of the short term unsecured credit.

24. Between January and April 1958, a series of discussions and negotiations took place between the Bank, acting principally by Mr. Julius Leof, a Vice-President, and the Company, acting by myself as its President. During those discussions and negotiations, the Exchange and the donation of Burlington stock were described and explained in detail by me to Mr. Leof, orally and in writing. As a result of those discussions and negotiations, and in large part based upon the increase of the capital of the Company effected by the Exchange and donation to over \$1,000,000, on or about April 11, 1958, the Bank granted to the Company an unsecured loan of \$400,000, at a rate of interest of one-half of one percent above the prime rate in Philadelphia. At no time prior to April 11, 1958 had the Bank granted unsecured credit over and above the amount of \$100,000. Never before had the Bank granted the Company unsecured credit at an interest rate less than one percent over the prime rate.



## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

25. Much of the sequence of the discussions and negotiations which led to this dramatic increase in the Company's credit with the Bank, based in large part on the increase in capital effected by the Exchange, is set out in an exchange of letters between Mr. Leof and myself, or our respective assistants. On December 30, 1957, I sent to Mr. Leof a copy of the accountants' report for the period ended November 30, 1957. I annex hereto as Exhibit F a copy of my letter. In it I informed Mr. Leof that I intended to explore with him the continued financing of the Company by the Bank and that, as soon as I was able to do so, I would send him the Company's year-end audited report for the year ended December 31, 1957. On January 2, 1958, Mr. Leof replied, stating that the Bank would "be very happy to meet with [me] when the annual figures are available and review the needs of [the] company for the current year." (A copy of his letter is annexed as Exhibit G.)

26. On February 14, I did send the 1957 year-end reports for the Company and Burlington, its affiliate (but not yet a subsidiary), to Mr. Leof. In the letter forwarding them I stated:

AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

"Would you please, once you will have studied the enclosed statements, suggest a date at your convenience for a meeting either in Philadelphia or in New York where we might discuss American Foam Rubber Corporation's financial program for the current year."

A copy of my said letter, dated February 14, 1958, is annexed hereto as Exhibit H.

In the several weeks following, we conferred by telephone and in person, on several occasions, discussing all aspects of the Company's plan to increase its capital to over \$1,000,000 by means of the Exchange and the donation of the Burlington shares.

27. On April 11, 1958, Mr. Leof wrote to me and informed me that the Bank had "established an unsecured line of \$400,000" for the Company. This is the loan described in paragraph "24" above. A copy of the said letter is annexed hereto as Exhibit I.

28. The relationship between the Bank's grant of the \$400,000 unsecured loan and the Exchange is demonstrated by the sequence of events in April 1958, reflected in the letters. The grant of the additional financing occurred immediately after a meeting between Mr. Leof and myself in Philadelphia, held shortly before April 11, 1958. At that



## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

meeting, I furnished to Mr. Leof the exact details of the Exchange and the related donation of Burlington shares. Mr. Leof asked for a written statement of the details of the Exchange and donation. In a letter dated April 14, 1958, a copy of which is annexed hereto as Exhibit J, I complied with his request:

"As I have communicated to you at our last meeting in Philadelphia, I am about to undertake the following legal steps to increase American Foam Rubber's capitalization to over one million dollars so as to qualify as soon as possible for the triple A-1 rating of Dun & Bradstreet:

1.) Merging Burlington Holding into American Foam Rubber Corp. in form of capital contribution by the owners of Burlington Holding to American Foam Rubber without receiving either payment or stock in exchange. This capital contribution will be undertaken based on market value without reevaluation. The market value will be determined by the amount paid by the present owners of Burlington to Mr. Samuel Buchman for his one-third interest on May 17, 1957. This will result in a capital contribution of \$120,000, the one-third interest having been acquired at \$40,000. Concurrently, we are going to have the real estate appraised and the difference between this amount of \$120,000 and the expected much higher evaluation might at a later date be added to capital in the form of upgraded reevaluation. I prefer to use this course to avoid that the auditors, with whom I have cleared this question, should mention in their future reports that part of the capital contribution is derived from upgraded valuation.

## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

2.) An amount of \$250,000 to \$300,000 of the bonds and/or officers' notes belonging to the present stockholders will be capitalized in the form of cumulative preferred shares yielding a 5% interest, which interest is the same as was paid on bonds and notes.

These changes in the capital structure of American Foam Rubber will, of course, have other salutary effects, namely, to substantially decrease long term debts and bring about a much better ratio between net worth and fixed assets and net worth and long term liabilities."

29. I respectfully submit that in and by the grant of the \$400,000 unsecured credit line, the Bank confirmed the fact that the Exchange and related donation of Burlington shares were precisely what they were intended to be -- the direct opposite of a step to take cash or cash realizable property out of the Company. Shortly after April 14, 1958 the Bank also specifically consented to the donation of Burlington shares, under provisions of the Term Loan Agreement, which included a requirement that it consent to any merger of the Company and Burlington, and one effectively forbidding purchase or redemption by the Company of the preferred stock issued under the Exchange. This point is discussed later in this affidavit.

C. The Exchange and the simultaneous donation of assets secured for the Company high credit ratings from Dun & Bradstreet, Inc. and the National Credit Office.



AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

30. The principal agencies with whom the Company dealt in 1957 and 1958 were Dun & Bradstreet, Inc. and the National Credit Office. One of the principal objects of the increase of the capital of the Company, by the Exchange and donation of Burlington shares, was to secure the highest credit ratings possible from those two agencies. In the latter part of 1957 and in early 1958, I, accordingly, advised Dun & Bradstreet, Inc. and the National Credit Office, 2 Park Avenue, New York, N.Y., of the Company's plans to increase its capital to over \$1,000,000 by the means described above. In late November 1957, I met with J. Warren Foley of the National Credit Office. In addition to presenting figures of the Company's operations as of October 31, 1957, I informed him of the contemplated Exchange and donation of the Burlington shares of stock. On November 29, 1957, he wrote to me informing me that our meeting enabled the National Credit Office "to place a well deserved top rating on American Foam." A copy of the said letter is annexed hereto as Exhibit K.

31. On February 17, 1958, I wrote to Mr. Foley, enclosing a copy of the Company's statement as at December 31, 1957. The text of my letter follows:

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"With reference to my letter to you dated December 3, 1957, I have the pleasure to send you a consolidated statement on the financial condition of American Foam Rubber Corporation and Wholly-Owned Subsidiaries as at December 31, 1957. This statement does not include the financial results of Burlington Holding Corp. which is the real estate company belonging to the same stockholders but which is not a subsidiary of American Foam Rubber Corporation.

Should you be interested in the financial results of this corporation, I would have no objection to communicate them to you. In any case, the stockholders of American Foam Rubber Corporation have the intention to merge the real estate corporation into the parent company and in so doing increase the capital investment of the parent company. Likewise, as I told you at our meeting, the stockholders have the intention of capitalizing a great portion of the long term bonds so as to bring the total capital of the company to over one million dollars not later than during this current fiscal year. (under-scoring supplied)

With my best regards,

Sincerely,

AMERICAN FOAM RUBBER CORPORATION

Alexander F. Pathy

AFP:dk  
Encl.

cc: Mr. Angelo Cecchi."

32. During the same period I communicated with Dun & Bradstreet, Inc., advising them likewise of the con-



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templated Exchange and donation. On or about March 14, 1958, Dun & Bradstreet issued an "Analytical Report", a copy of which is annexed as Exhibit L. That report repeated information from prior investigations, and set forth the following as Dun & Bradstreet's findings:

"Current Investigation: Interviewed February 25, 1958 Alexander F. Pathy, President, reported that the period of large expenditures for plant and equipment remodernization is now behind the concern and projections show that profit yield will be of good proportions. Pathy stated it continues to be the intention of management to retain all profits with these funds now going towards the development of increased working capital. He said that 1958 plans also call for the conversion of certain of the bond indebtedness to either capital stock or capital surplus. Thus it was indicated that a good sized growth can be expected in both working funds and net investment during 1958 with the position gradually trending towards increased liquidity." (underscoring supplied)

33. By May 27, 1958 the Exchange and donation of Burlington stock had been completed. A report was issued on May 28, 1958; a copy thereof is annexed hereto as Exhibit M. I respectfully direct this Court's attention to page 5 of the report setting forth the reduced debentures and note debt, the \$300,000 capital item on account of preferred stock, and the \$120,000 "capital surplus" item, representing the

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donation of the Burlington shares. I also respectfully direct this Court's attention to the following paragraphs of the "Analysis", appearing on pages 6 and 7 of the report:

"The figures as at March 30, 1958 represents the interim Pro-Forma consolidated financial position of the company, giving effect to certain changes which took place during April, 1958. These changes included the acquisition by the company of a former affiliate corporation, Burlington Holding Corp., as a subsidiary, the stock of said newly acquired subsidiary being donated by its stockholders and resulting in the creation of the capital surplus account of \$120,000. In addition, this balance sheet gives effect to the conversion of \$231,000 Series "A" and Series "B" debentures and \$69,000 in notes payable to equity capital represented principally by preferred stock."  
(underscoring supplied)

\* \* \*

"As previously mentioned, certain important changes occurred during April, 1958, highlighted by the conversion of about half of the funded debt into equity capital and the acquisition of the capital stock of a former affiliated company. As a net result, tangible net worth showed material expansion and correspondingly, fixed assets showed an increase of about \$150,000 over year end 1957, representing the real estate and equipment of the newly acquired subsidiary, Burlington Holding Corp. Net working capital, as shown at March 30, 1958 was light, but during April, 1958 the company obtained a line of unsecured bank credit of close to medium six figures from an out of town bank. According to the management, the company, has, so far, borrowed \$300,000 against this line and which has provided the necessary working funds to continue operations in a satisfactory manner." (underscoring supplied)

\* \* \* \*



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"(2) Debentures: Series "A" debentures originally issued May 1, 1950 and due May 1, 1960 and Series "B" debentures issued August 1, 1955 and due August 1, 1965 are held by the stockholders and bear interest at 5%. There is no designated security and there are no sinking funds arrangements. At December 31, 1957, outstanding debentures totaled \$343,000. During April, 1958, \$201,000\* of these debentures were converted into capital stock and were represented by a certain portion of preferred shares. The remaining debentures, consisting of both Series "A: and Series "B" continue to be held by the stockholders and are due respectively, May 1, 1960 and August 1, 1965." (underscoring supplied)

"(3) Notes Payable: At December 31, 1957, notes payable to stockholders and other totaled \$125,000, bearing a due date of January 2, 1959. During April, 1958, \$69,000 of these notes payable were converted into capital stock and were represented by a certain portion of preferred shares. The balance of the notes payable totaling \$56,000 continue to be due January 2, 1959." (underscoring supplied)

34. The May 28, 1958 report by Dun & Bradstreet, Inc., in addition to featuring in its "analysis" the increase of capital resulting from the Exchange and the donation of Burlington shares, set forth the rating change based thereon. In the upper right hand corner of the report this Court will see the legend, "Rating Change". The actual "Rating" appears approximately one quarter down the page, as follows:

\* This is an error by Dun & Bradstreet, Inc. The correct figure is \$231,000.

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"RATING: N.Q. Branch of Burlington, N.J.  
to A+ 1 Also Burlington, N.J."

This rating of "A+ 1" should be contrasted with the absence of a rating, indicated by the dash (-), after the term "RATING" on the report of March 14, 1958, a copy of which is Exhibit L.

35. From the copy of the "Key to Ratings" by Dun & Bradstreet, Inc. outstanding in 1958, annexed hereto as Exhibit N, it will be seen that the rating consisted of two components: a) the "estimated financial strength", and b) the "composite credit appraisal." The "estimated financial strength" meant the "capital," the highest of which was Aa, meaning over \$1,000,000, and the second highest of which was A+, meaning over \$750,000. The "composite credit appraisal" referred to the promptness with which the company being rated paid its debts. The highest was "A1." The next highest was "1." Primarily based upon the increase of capitalization effected by the Exchange and the donation of Burlington shares, the Company achieved the second highest composite credit appraisal, "1", as well as the second highest rating of estimated financial strength, "A+."



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36. As stated above, the "A+" estimated financial strength rating, achieved in May 1958, was for a capital of over \$750,000, the highest being "Aa", for a capital of over \$1,000,000. The Company did achieve the "Aa" estimated financial rating in March 1959. I annex hereto as Exhibit O a copy of the Dun & Bradstreet, Inc. report of March 20, 1959. The Court will note the legend "Rating Change" at the top of the first page, and the actual rating change of "A+1" to "Aa1" at the middle of the page. The reason why the Company was not given the "Aa" estimated financial strength rating in 1958 was because Dun & Bradstreet, Inc. required audited year-end statements reflecting the \$1,000,000 plus net worth, which were not available until early 1959.

37. The Court will also note the "Summary," in bold face type, at the very outset of the report of March 20, 1959:

"This company during the last several years engaged in an extensive plant expansion program financed by internal and external means. Moderate earnings and additional investment in capital stock together with recent conversion of debentures into equity capital has resulted in substantial growth in tangible net worth. Balance sheets are characterized by a sizable investment in plant and inventories. While working capital

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appears light, the company has supplemented its funds when necessary through the use of sizable unsecured bank loans. Bank and trade comment favorable." (underscoring supplied)

The "Analysis" contained substantially the same comments concerning the Exchange and the donation of Burlington shares as those set forth in the report of May 28, 1958.

38. I respectfully submit that the aforementioned credit reports prove that to this leading credit agency, Dun & Bradstreet, Inc., and to the persons and organizations throughout the business world who relied on it for measuring what credit they would extend, the Exchange and the simultaneous donation accomplished an enormous improvement in AFR's financial worth and strength. It would have been an incredible act of folly and futility on the part of the INDIVIDUAL DEFENDANTS to accomplish this with any intent of then undoing it by using the Exchange as a means of siphoning cash or cash realizable assets from AFR. The fact is, of course, that the Exchange could not have been so used; nor was there any thought of ever doing so.

- D. The Exchange seriously disadvantaged the INDIVIDUAL DEFENDANTS with respect to obtaining "cash - or cash realizable property - from the corporation."



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39. In achieving the purpose of strengthening the financial condition and standing of the Company, by the Exchange, MRS. de MONTMOLLIN substantially lessened her own rights and opportunities to receive cash or cash realizable property for the \$300,000 investment, changed in nature and form by the Exchange. The preferred stock received was equity; the debentures and notes surrendered were debt. Neither the debentures surrendered nor the preferred stock received contained any unusual provisions which affected this subordinate position of the stock. I annex hereto, as Exhibit P a copy of the form of the certificates of preferred stock received, and as Exhibit Q a copy of the form of the debentures surrendered. I respectfully direct this Court's attention to the following aspects of the rights of the holders of each class of securities, all of which are, I believe, significant in determining whether the Exchange was or could have been part of "a plan to obtain cash -- or cash realizable property -- from the corporation:"

(a) Under the debentures, interest, at the rate of 5% per annum, was payable semi-annually, on April 1 and October 1 of each year. The preferred stock certifi-

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cates, of course, made no provision for interest. Dividends were payable at the rate of 5% per annum "when and as declared by the Board of Directors ... but only out of net profits or net assets of the Corporation legally available therefor."

The payment of the interest under the debentures was a fixed, unconditional obligation. Failure to pay constituted a default. As at April 1, 1958, MRS. Je MONTMOLLIN was entitled to the payment of a semi-annual installment of interest on the \$231,000 face amount of debentures that she surrendered for the preferred stock, amounting to \$5775. A like payment was due on October 1, 1958 and on April and October 1 thereafter. She never received any of these cash payments, because she exchanged the debentures for preferred stock. She was, likewise, entitled to interest on the notes, which she never received.

Under the preferred stock certificates, dividends, at the same rate of 5% per annum, were to be paid "when and as declared by the Board of Directors" and to the extent legally permissible. I am informed that such dividends would have been legally permissible in 1958, and 1959. Sometime in 1960, when the large operating losses suffered in 1959 and 1960, hereinafter discussed, wiped out



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both earned and capital surplus, such dividends became, I am informed by my attorneys, illegal. The fact is, however, that no dividends ever were declared, because the dominant concern of the INDIVIDUAL DEFENDANTS was building up and maintaining the capital of the Company.

(b) Payments on the principal of the debentures were required at the rate of 5%, likewise on April and October 1 of each year, if "earnings and profits at least sufficient in amount to provide" for such payments were accumulated. "Earnings and profits" were defined to "mean accumulated profits less all taxes, dividends and payments on account of principal of said debentures."

This payment-of-principal provisions of the debentures should be compared to the redemption provisions of the preferred stock certificates, which contained no requirement of redemption, partial or complete. They only permitted redemption, in whole or in part, when authorized by the Board of Directors. No such redemption was ever authorized or even considered. Redemption of any capital

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stock, in excess of an aggregate nominal amount of \$10,000 would have been, however, a breach of covenant under the provisions of the Pennsylvania Bank loan agreement, hereinafter detailed, which would have been fatal to the Company.

(c) Prepayment of the debentures was permitted at any time, in whole or in part, and there was no restriction in the terms of the debentures, or in any other instrument, on the Company's purchasing the debentures. I am informed by my attorneys that no provision or rule of law restricted or forbade prepayment, in whole or in part.

On the other hand, purchase of the preferred stock was subject to the legal restrictions on impairment of capital discussed in the accompanying memorandum. It was also out of the question, except to the extent of \$10,000 under the Pennsylvania Bank Term Loan Agreement discussed below.

(d) The debentures were due and payable, absolutely, on their due dates. Of the \$231,000 face amount of debentures held by MRS. deMONTMOLLIN and exchanged for preferred stock, \$63,000 face amount were due on April 1, 1960 and \$168,000 due on August 1, 1965. There was thus an



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absolute right of MRS. de MONTMOLLIN to be paid \$63,000 cash on April 1, 1960 and \$168,000 on August 1, 1965, which, by the Exchange, she gave up for the rights of a holder of preferred stock of the Company, which did not include any right to redemption, and only permitted it subject to legal restrictions and to the restrictions of the Pennsylvania Bank Loan Agreement.

- E. Under the agreement between the Company and the Pennsylvania Bank, governing until December 1959, the INDIVIDUAL DEFENDANTS and the Company were unable to use the Exchange as a means of obtaining cash or cash realizable property from the Company.

40. I have heretofore referred to the Term Loan Agreement between the Company and the Pennsylvania Bank. That agreement, as, upon information and belief, many bank loan agreements, contained a number of covenants of the borrower, both affirmative and negative, designed to maintain the financial soundness of the borrower, to inform the Bank of developments affecting the borrower's financial condition and to require the Bank's consent to several kinds of transactions out of the ordinary course of

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business. Most of these covenants were set forth in Section 4 of the Agreement, a copy of which is annexed hereto as Exhibit B.

41. I respectfully direct this Court's attention to the first unnumbered paragraph of Section 4 and to subsections 4.11 and 4.13 of that section, quoted below:

"Each of the Borrowers covenants and agrees that during the entire time that this agreement is in effect and thereafter so long as any portion of the principal of or any interest upon any Note given pursuant to this agreement remains unpaid, it will:

"4.11 Refrain from purchasing or redeeming any of the capital stock of either of the Borrowers or of any of their subsidiaries if the aggregate consideration for all of such purchases and redemptions exceeds \$10,000 in money or property." (underlining supplied)

"4.13 Refrain from merging or consolidating with any corporation or permitting any subsidiary so to do, provided that the Borrowers may merge or consolidate with each other or with any subsidiary."

Section 5 of the agreement defined "Events of Default" under the agreement. Six categories of acts or failures to act, of the Company, were made events of default, the first four of which (the last two concerned receivership, bankruptcy and related events) are set forth below;



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"5.1 Failure of Borrowers to pay any quarterly installment of principal of the Permanent Note within ten days after the same becomes due.

"5.2 The failure of Borrowers to pay any installment of interest upon any Temporary Note or upon the Permanent Note for a period of ten days after such installment becomes due.

"5.3 Any representation or warranty made in this agreement or any financial statement or other information or report furnished pursuant to this agreement proves to be incorrect in any material respect.

"5.4 The breach on the part of Borrowers in performance of any other provision of this agreement and the failure to cure such breach within 30 days after written notice thereof by Bank."

Section 6 of the agreement stated the Pennsylvania Bank's rights upon default:

"6.1 In the event of the occurrence of any default as defined in Section 5, then and in any such event at the option of the Bank the principal of and accrued interest upon all Temporary Notes then outstanding or the Permanent Note if then outstanding shall become immediately due and payable without demand, presentation or notice of any kind and the obligation of Bank to make any further loans under this agreement shall cease and terminate, anything in this agreement or in any of such Notes to the contrary notwithstanding."

42. The significance of the provisions concerning redemption or purchase of any shares of stock by the

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Company is clear. Had the INDIVIDUAL DEFENDANTS used the Exchange as "a first step in a plan to obtain cash - or cash realizable property - from the corporation" to the extent of more than the nominal \$10,000, by way of the redemption or purchase by the Company of any of the shares of preferred stock issued to MRS. de MONTMOLLIN under the Exchange, or any other shares of stock, the Company would have committed an act of default upon which the Pennsylvania Bank would have had the right to call the entire amount owed to the Bank immediately due and payable. I respectfully submit that using the Exchange as "a first step" or as any step "in a plan to obtain cash - or cash realizable property - from the corporation" would have been utterly senseless. The purpose of the Exchange was to improve the Company's standing and credit, not to render one of its largest obligations immediately due and payable.

43. I have pointed out the impossibility of my and the other INDIVIDUAL DEFENDANTS having used the Exchange to obtain cash or cash realizable property by means of redemption or purchase by the Company of the shares of preferred stock. Dividends upon any class of stock were,



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as redemption and purchase, restricted by the Pennsylvania Bank Loan Agreement. Under Section 4.8, the Company was obligated to:

"Refrain from declaring or paying upon any class of its capital stock now or hereafter outstanding dividends which in the aggregate for both of the Borrowers would exceed \$25,000 in any fiscal year except dividends payable solely in the capital stock of the Borrowers or either of them."

44. The Company was thus permitted, by the loan agreement, to pay dividends upon the preferred or the common stock of up to \$25,000 per year. The preferred stock, however, carried no greater rights to dividends, vis-a-vis either the Pennsylvania Bank or the debenture holders, including BUCHMAN, than the common stock. Thus the INDIVIDUAL DEFENDANTS were gaining no advantage with respect to dividends by the creation and issuance of shares of a new class of preferred stock. If they wished to distribute to themselves cash or cash realizable property, by way of dividends, the Exchange was not needed or at all helpful in doing so. The Exchange, therefore, could not have been a "first step", or any step, in any "plan to obtain cash -- or cash realizable property -- from the corporation" by the dividends means. And the fact is, of course, there never

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was any consideration or suggestion of dividends on any class of stock, and none ever were declared, between May 17, 1957 and February 1961, when the Company was adjudicated bankrupt.

F. Under the agreements with Walter E. Heller & Co., Inc., which succeeded the Pennsylvania Bank as a source of financing, the same disability continued, until the bankruptcy of the Company.

45. The loans by Pennsylvania Bank were not paid off by the Company, and it was not released from the Pennsylvania Bank loan agreement restrictions, until December 29, 1959, four weeks after the Company assumed equally stringent obligations under another agreement. On that date the Company paid to the Pennsylvania Bank the amount of the Company's indebtedness to it, by turning over part of the proceeds of a loan to the Company by Walter E. Heller & Co., Inc. (hereafter in this and accompanying papers referred to as "Heller"). Earlier in 1959, I had entered into negotiations with Heller looking towards its factoring the Company's accounts receivable and otherwise lending it financial aid. The said negotiations culminated in the execution of a basic financing agreement dated December 3, 1959, and a series of related loan and mortgage agreements



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(hereafter in this and accompanying papers referred to as the "Heller Agreements"). Because of their length, I do not annex hereto a copy of each of the Heller Agreements. I do respectfully direct the Court's attention to several specific provisions of the said agreements bearing upon the issue before this Court of whether, after December 29, 1959, the Exchange was or could have been a step in a plan to take cash or cash realizable property from the Company.

A. The basic loan agreement contained a number of warranties by the Company concerning its financial condition. Among such warranties was a warranty:

"that the financial statements dated July 19, 1959, heretofore furnished by Borrower to Heller, fairly reflect the financial condition of Borrower and its said subsidiaries on a consolidated basis, and that since the date of said financial statements there has been no material adverse change in the financial condition of Borrower except that for its fiscal year ending January 3, 1960, it will sustain an aggregate loss of approximately \$250,000."

The "financial statements" referred to included a balance sheet setting forth the long term debt of the Company and its capital reflecting the results of the Exchange. Had the Company somehow redeemed or purchased any of the shares of preferred stock exchanged for debentures, or the INDIVIDUAL DEFENDANTS otherwise used the

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Exchange as a first, or a later, step, in "a plan to obtain cash -- or cash realizable property -- from the corporation", the statements furnished to Heller would have been materially false. Such falsity would have constituted "a material breach of [the] agreement", granting Heller the right to call all indebtedness (which, after December 29, 1959, was never less than \$555,000) immediately due and payable, and foreclose on all collateral security held by it, which included a real property mortgage on the principal plant, chattel mortgages on most of its equipment, and pledges of most of its inventories and accounts receivable.

B. Both an inventory loan agreement, providing for collateralizing the Company's inventories, and a collateral note executed pursuant to the inventory loan agreement, provided that:

"if for any reason the payee or holder hereof in its opinion shall deem itself insecure, the holder may, without notice or demand, declare the entire amount of this note and all other indebtedness or liabilities of the undersigned to the holder to be immediately due and payable and proceed to collect and enforce the same at once."



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Any such use of the Exchange to take cash or cash realizable property out of the Company, had such a suggestion ever been made or had it ever occurred to me, would have been reason for Heller to call due the entire indebtedness of AFR. Neither ever occurred. On the contrary, I specifically recall informing Heller officers, in December 1959, of the intention of the INDIVIDUAL DEFENDANTS to again do the precise reverse of taking cash or cash realizable property from the Company, to invest additional large amounts in the capital of the Company by purchasing additional shares of preferred stock. This is confirmed by the affidavit of Herbert E. Ruben, Esq. That additional large investment of \$145,000, by the purchase of 1450 shares of preferred stock, is hereinafter discussed.

C. Under the Heller Agreements Heller obligated itself to make a loan in a definite amount only with respect to a \$500,000 term loan, secured by a real estate mortgage, chattel mortgage and other collateral. Loans against receivables and inventory were not specified as to amount. Heller retained the right to halt the making of loans against inventory and receivables whenever it so determined. Upon information and belief, if the Company, at

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any time after it entered into the Heller Agreements, had proceeded to purchase or redeem any of the shares of the preferred stock, Heller would have immediately cut off further loans. Heller would have been lost to the Company as a source of financing. The fact, of course, is that no thought ever occurred to the INDIVIDUAL DEFENDANTS to have the Company purchase or redeem any of the shares of preferred stock, or to pay dividends thereon, to use the preferred stock, as "a first step", or any step, in "a plan to obtain cash -- or cash realizable property -- from the corporation."

46. The Pennsylvania Bank indebtedness was paid off on December 29, 1959. On that date Heller advanced to the Company \$500,000 under the term loan provided for in the Heller Agreements and \$55,000 under an Inventory Loan Agreement. \$355,000 of the said loans was not paid to the Company but was paid by Heller to the Pennsylvania Bank. The transactions are described in a memorandum of Herbert Ruben, Esq., an officer of and counsel to Heller, which is discussed below. Thus the restrictions of the Pennsylvania Bank loan agreement, discussed above, were in force until four weeks after the restrictions of the Heller Agreements



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went into effect. The restrictions under both would have rendered use of the Exchange as part of "a first step", or any step, in "a plan to obtain cash -- or cash realizable property - from the corporation" an act of ruin, thwarting the very purposes of the Exchange.

- G. After the Exchange the INDIVIDUAL DEFENDANTS never used or even considered using the Exchange as a "first step in a plan to obtain cash - or cash realizable property - from the corporation"; every aspect of the Exchange and related further action was to serve and did serve a directly contrary purpose.

47. The purpose of the Exchange - to strengthen the financial condition and standing of the Company - has been explained. The Exchange and the simultaneous donation to the Company by the INDIVIDUAL DEFENDANTS of their Burlington shares increased the capital and net worth by \$420,000 and gained the desired Dun & Bradstreet rating for the Company. In the year 1959, the Company suffered from insufficiency of working capital. The financing agreements with Heller were negotiated and entered into to secure working funds. Toward the end of 1959 it also became clear that, because of operating losses, the capital and net worth of the Company would fall below \$1,000,000 and the Company

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would lose its favorable Dun & Bradstreet rating, unless additional capital contributions were made by the INDIVIDUAL DEFENDANTS.

48. During the first nine months of 1959 the Company suffered a net loss of \$111,512 according to financial statements prepared by Edward Isaacs & Company. I annex hereto as Exhibit R, a copy of the balance sheet of the Company as at October 11, 1959, taken from the said statements. I respectfully direct this Court's attention to the capital account which, as at October 11, 1959, had fallen, as a result of the losses in the period from January 5 to October 11, 1959, to \$991,128. This was below the one million figure necessary to maintain the Dun & Bradstreet, Inc. rating achieved in 1959 by means of the Exchange. Losses continued in the last three months of 1959. It became necessary to again add to capital, by investment by the INDIVIDUAL DEFENDANTS. In order to do so it was necessary to amend the Company's certificate of incorporation again so as to increase the authorized number of shares of preferred stock by an additional 2000 shares. The necessary corporate action was taken at meetings of the Board of Directors and of the stockholders of the Company, held on December 22 and 23, 1959, respectively.



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49. On or about December 29, 1959, the additional investments were made. General Industrial Supply Corp., a corporation, all of the outstanding capital stock of which was owned by MRS. de MONIMOLLIN, my brother and myself, purchased 1200 shares of preferred stock for \$120,000. MRS. de MONTMOLLIN purchased 250 shares for \$25,000. On or about December 29, 1959, during the course of a meeting between MRS. de MONTMOLLIN and myself and Herbert E. Ruben, Esq., counsel and an officer of Heller, at the Company's offices in the Empire State Building, I informed Heller of the additional capitalization. On that same day, as hereinbefore noted, Heller opened the Company term loan provided for by the Heller Agreements, and the Pennsylvania Bank loan was paid off. My statement concerning the additional investments by the INDIVIDUAL DEFENDANTS is referred to in a memorandum of the meeting, by Mr. Ruben, dated December 30, 1959. Mr. Ruben's memorandum, a copy of which is annexed hereto as Exhibit S, stated in part:

"He stated that he was going to improve his balance sheet picture by convering approximately \$145,000 in current liabilities owing to stockholder interests into preferred stock."  
(underscoring supplied)

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The accuracy of the copy of Mr. Ruben's memorandum of December 30, 1959, and of the statements therein contained, are attested to in the accompanying affidavit of Mr. Ruben.

50. I also annex hereto as Exhibit T a copy of another memorandum by an officer of Heller, one dated January 6, 1960, by Charles E. Weaver, then a Vice President of Heller. I respectfully direct this Court's attention to the following portion of Mr. Weaver's memorandum:

"In addition, Dr. Pathy and Marie Louise DeMontmollin, the principal stockholders, plan to invest an additional \$100,000.00 in cash in the company taking in exchange, preferred stock. Their purpose in doing this is to keep the net worth of the business above \$1 million in spite of the contemplated losses in 1959 since they are most averse to retain their AAL Dun & Bradstreet rating, and they feel it is necessary to show a net worth in excess of \$1 million on their year-end balance sheet to accomplish this aim." (underscoring supplied)

The accuracy of the copy of the statements are likewise attested to in and by the accompanying affidavit of Herbert E. Ruben, Esq.

51. With the additional investment of \$145,000 by the INDIVIDUAL DEFENDANTS, the Company was able to



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maintain the Dun & Bradstreet rating. In 1960, however, the Company suffered huge operating losses, calculated by Edward Isaacs & Co to be close to one million dollars. At some point during the year the losses consumed the entire earned and capital surplus rendering illegal any dividends on, or redemption or purchase by the Company of, any shares of stock. The law, as well as the Heller agreements, forbade using the preferred stock to obtain cash or cash realizable property from the Company.

52. In July and August of 1960, a total of \$70,000 additional cash was invested in the Company by General Industrial Supply Corporation and other companies, all of the capital stock of which was owned by my brothers and myself. The investments took the form of loans to the Company, evidenced by promissory notes, all payable on December 30, 1961. A schedule of the investments follows:

<u>Date</u>	<u>Lender</u>	<u>Amount</u>
July 25, 1960	General Industrial Supply Corporation	\$25,000
July 27, 1960	Pathy Lines, Inc.	20,000
July 27, 1960	Atlantic Commerce and Shipping Company, Inc.	20,000
August 3, 1960	General Industrial Supply Corporation	5,000

## AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968

The loans were not paid. In January 1961 the Company was compelled to file its arrangement petition. In February 1961 it was adjudicated bankrupt. Each of the above described loans is the subject of a proof of claim filed with the Referee in Bankruptcy herein, to which no objection has been made.

53. The loans made in 1960, described above, brought the total investments in the Company, since May 1957, by the INDIVIDUAL DEFENDANTS to \$635,000. A breakdown of the total amount follows, by date, nature of investment, and amount:

<u>Date</u>	<u>Nature of Investment</u>	<u>Amount</u>
May 27, 1958	the Exchange	\$300,000
May 27, 1958	donation of Burlington stock	120,000
December 29, 1959	purchase of additional shares of preferred stock	145,000
July 25, 1960	Loan	25,000
July 27, 1960	Loans	40,000
August 3, 1960	Loan	<u>5,000</u>
		\$635,000

Not one dollar of the said investments has been repaid to the INDIVIDUAL DEFENDANTS, by way of inter-



AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968  
est, return of principal, dividends, or redemption or purchase  
of stock. Nor is there any possibility of any recovery from  
the Company of any of the amounts invested in the preferred  
stock, aggregating \$565,000. On the \$70,000 in loans there  
may be a small dividend from the bankruptcy estate.

I also want to point out to this Court that,  
in addition to the investments described above, the  
INDIVIDUAL DEFENDANTS paid to BUCHMAN, between May 17, 1957  
and January 2, 1959, for the shares of common stock of AFR  
alone, which they bought from BUCHMAN under the Buy-Sell  
Agreement, the total amount of \$183,220.

54. I respectfully submit that the Exchange  
was not and could not have been, in its purpose or effect,  
"a first step", or any step, in "a plan to obtain cash --  
or cash realizable property -- from the corporation", and

AFFIDAVIT OF ALEXANDER PATHY, SWORN TO MARCH 5, 1968  
that the INDIVIDUAL DEFENDANTS are entitled to summary  
judgment dismissing the second cause of action of BUCHEMAN's  
Complaint.

Sworn to before me this  
5<sup>th</sup> day of March, 1968.

/s/ALEXANDER F. PATHY  
ALEXANDER F. PATHY

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**Notary Public**

CECILIA W. KRUDOP  
Notary Public, State of New York  
No. 41-22037-85  
Qualified in Queens County  
Commission Expires March 30, 1969.



## STIPULATED FACTS.

the United States Court House, Foley Square, New York, N. Y. The minutes of the said meeting, a copy of which is marked as Defendants' Exhibit 15 on the pre-trial depositions, correctly set forth the appearances and proceedings at the said meeting.

56. The following table sets forth the names and periods of service of all of the directors and officers of AFR from January 1, 1956 to May 17, 1957:

Directors: Samuel Buchman, Alexander F. Pathy and Marie de Montmollin.

President:	Samuel Buchman*
Executive Vice President:	Alexander F. Pathy
Vice President:	Felix Buskey
Secretary:	Alexander F. Pathy
Treasurer:	Marie de Montmollin

Additional Vice Presidents: Marie de Montmollin and Suzanne M. Pathy between November 8, 1956 and May 17, 1957.

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\*Buchman resigned as President on May 17, 1957 and was succeeded on that day by Pathy.

## STIPULATED FACTS

III. (a) The parties stipulated, for the purpose of the trial of the second cause of action in the complaint, the first counterclaim in the answer of defendant Ackman and the counterclaims in the answer of the three individual defendants, that the following facts are not in dispute (each party reserving the right to object to any such stipulated fact on any of the grounds enumerated in IV[b] infra), American Foam Rubber Corporation referred to in the complaint being referred to as "AFR":

A. General.

1. At all times mentioned in the pleadings and since March 6, 1950, when it was incorporated, AFR was a corporation organized and existing under and by virtue of the Laws of the State of New York.

2. On or about January 17, 1961, AFR filed a voluntary petition for an arrangement under Chapter XI of the Bankruptcy Act of the United States.

3. On or about February 21, 1961, AFR was on said petition duly adjudicated a bankrupt in the United States District Court for the Southern District of New York; and on February 23, 1961, Milton R. Ackman (hereinafter the "Trustee") was appointed Trustee in Bankruptcy of AFR and he has at all times since been and now is acting as such Trustee.



## STIPULATED FACTS

4. By order of this Court, made by Hon. Robert P. Stephenson, Referee in Bankruptcy, dated June 16, 1961, the Trustee was duly authorized to assert and prosecute the first counterclaim in his answer.

5. The Trustee has insufficient assets in his hands to pay in full the liabilities of said bankrupt.

6. Samuel Buchman, original plaintiff herein, died November 4, 1965, whereupon plaintiffs herein were duly appointed and since have been acting as executors of his estate. Said Samuel Buchman is hereinafter referred to as "Buchman".

7. At all times mentioned in the pleadings, AFR was engaged in the manufacture of foam rubber and foam rubber products and had its executive offices in the Empire State Building in the Borough of Manhattan, City of New York, and its machinery and equipment in a parcel of improved real estate located in Burlington, N. J. From the time of incorporation of each of the following corporations, AFR operated by and through it:

(1) Burlington Holding Corp. ("Burlington Holding" hereinafter), a New York corporation, incorporated May 15, 1950, holding title to the said parcel of improved real estate;

## STIPULATED FACTS

(11) Burlington Workshops, Inc., a New York corporation, incorporated February 10, 1958, conducting a work shop located in said improved real estate;

(111) Mirafoam Industrial Sales, Inc., a New York corporation, incorporated November 24, 1952, engaged in selling to wholesalers and manufacturers the products of its parent corporation;

(1v) Mirafoam Industrial Sales of Illinois, Inc., a Delaware corporation, incorporated April 23, 1953, engaged in selling to wholesalers and manufacturers the products of its parent corporation;

(v) Mirafoam, Inc., a New York corporation, incorporated November 24, 1950, engaged in selling to retailers the products of its parent corporation and of another subsidiary, Riverside Industries, Inc.; and

(vi) Riverside Industries, Inc., a New York corporation, incorporated January 14, 1955, engaged in sewing operations for the subsidiary, Mirafoam, Inc.

Burlington Holding became a wholly owned subsidiary of AFR on April 30, 1958 and each of the other five corporations was organized by AFR as its wholly owned subsidiary; all



## STIPULATED FACTS

six of said corporations continued, thereafter to beyond bankruptcy adjudication of AFR, as wholly owned subsidiaries of AFR. Each of said corporations, at all times mentioned in the pleadings, had its executive offices in the executive offices of AFR and had the same officers and directors as AFR. The first four of said subsidiaries discontinued business when AFR was adjudicated a bankrupt and thereafter, on February 26, 1964, made assignment for the benefit of creditors under New York law. The latter two filed petitions for arrangement under Chapter XI of the Bankruptcy Act when AFR did likewise and were thereafter taken over by purchasers.

8. AFR was organized in 1950 under the laws of the State of New York, with an original capitalization of approximately \$75,000, invested by three groups in approximately equal shares, each of which purchased one-third of the Class A common (voting) stock. The groups were: (1) Buchman, (2) a Charles Wyman and others of the Wyman family, and (3) Cornelius Egry (father of defendant Marie Louise de Montmollin), and the investment firm of Amsinck Sonne & Co., Egry purchasing 2/9ths and Amsinck Sonne & Co. 1/9th.

9. At or about the same time that AFR was organized, Burlington Holding was organized under the laws of the State of New York. It thereafter, and until January

## STIPULATED FACTS

17, 1961, held title to and leased to AFR improved real property located in Burlington, New Jersey, which was used by AFR for its manufacturing operations. At all times from its organization until April 30, 1953, the capital stock of Burlington Holding was owned by the owners of the Class A common stock of AFR in substantially the same proportions.

10. From the organization of AFR in 1950 until May 17, 1957, Buchman was the president and operating head of AFR and worked full time for it. The location of its principal plant was, at all such times, in Burlington, New Jersey. Until 1956, none of the other principal stockholders of AFR worked full time for it.

11. In or about 1951, AFR employed a Felix Buskey to assist in the organization of its production operations. From 1952 to the commencement of operation of the Industrial Division of AFR, Buskey was in charge of production.

12. On or about March 15, 1953, Cornelius Egry died. Defendant Marie Louise de Montmollin was the sole legatee under his Last Will and Testament and inherited his stock interest in AFR.

13. In 1953, Alexander F. Pathy and his wife, Suzanne M. Pathy, bought the 1/9th interest in the Class A common stock of AFR held by Amsinck Sonne & Co.



## STIPULATED FACTS

14. As of the end of 1953, the Class A common stock of AFR was held in approximately equal shares by (1) Buchman, (2) the Wymans, and (3) Marie Louise de Montmollin and the Pathys (hereinafter sometimes referred to as the "Pathy Group").

15. In late 1953, when defendant Alexander F. Pathy became vice president, secretary and a director of AFR, he began to spend a portion of his working time with it. He continued to spend a portion of his working time with AFR in 1954. During 1955, he gradually increased his time spent with AFR. In or about 1956, Pathy assumed the office of executive vice president and began spending substantially his full working time with AFR, in charge of the Retail Division of AFR.

16. In or about July 1954, the Wymans sold their interests in AFR to the other two groups, consisting of Buchman and the Pathy Group. The Wymans and their nominees resigned as officers and directors of AFR. Some of the shares of Class A common stock sold by the Wymans were purchased by Buchman and some were purchased by the Pathy Group. Upon the said sale of their shares by the Wymans, Buchman owned 40% and the Pathy Group 60% of the said common stock.

B. Facts Relating to the Establishment and Commencement of Operation of the Industrial Division of AFR.

## STIPULATED FACTS

17. In early 1955, in connection with the proposed establishment of the Industrial Division, it was determined by all of the then directors and officers of AFR that additional financing of AFR would be necessary, to be achieved by increase of its capital through sale of additional shares of its Class A common stock and by borrowing additional funds.

18. Thereafter, and in or about July 1955, the capital of AFR was increased by the purchase by Buchman and the Pathy Group of additional shares of the Class A common stock of AFR.

19. Upon the said purchase of additional shares of the said Class A common stock, Buchman became the owner of 1/3d, some of which he later transferred to his son, A. Sander Buchman, and the Pathy Group the owner of 2/3ds of all of the issued Class A shares.

20. For the borrowing of additional funds, AFR, together with Burlington Holding, on or about July 14, 1955, entered into an agreement with the Pennsylvania Company for Banking and Trusts (hereinafter referred to as "Pennsylvania Bank"), under which the Pennsylvania Bank agreed to lend to AFR from time to time amounts not exceeding in the aggregate \$400,000. A true and correct copy of said agreement is marked as Defendants' Exhibit B on the pre-trial depositions.



## STIPULATED FACTS

21. Earlier and in connection with the planned expansion of AFR's operations and the establishment of the Industrial Division, AFR, in 1954, engaged A. Sander Buchman, son of Buchman, as an engineer, to assist Felix Buskey in production operations.

22. On or about January 1, 1956, Howard Herbert was engaged as sales manager of AFR. He was charged, among other duties, with that of assisting in the development of an industrial foam rubber production and sales program, to go into effect upon the establishment of the Industrial Division.

23. In early 1956, it was determined by all of the then officers and directors of AFR to adopt, for the most important areas of sales of industrial foam rubber to be manufactured by AFR, a direct sales method under which sales in the said areas would be handled by salesmen in defined territories, working full time for AFR on a commission basis.

24. Upon the said determination to have most of the important areas of sales by the Industrial Division handled by such salesmen, AFR engaged the following salesmen for the following territories, which territories are

## STIPULATED FACTS

more precisely defined in the agreements hereinafter referred to in item 25:

Louis Levy, for the Metropolitan New York City  
Area

Irving Mirsky, for the Philadelphia and the New  
England Area

Donald B. Parker, for the Area of Ohio, Pennsylvania  
and several adjoining and nearby states

Helmut R. Spitzer, for the Midwest Area.

25. Each of the said salesmen was engaged, pursuant to a written employment agreement setting forth, among other things, the area and the rates of commission. True and correct copies of said employment agreements are marked as exhibits on the pre-trial depositions heretofore taken, as follows:

Agreement between AFR and Irving Mirsky, dated  
December 3, 1956 - Plaintiff's Exhibit 47

Agreement between AFR and Louis Levy, dated  
July 30, 1956 - Plaintiff's Exhibit 48

Agreement between AFR and Donald Parker, dated  
August 14, 1956 - Plaintiff's Exhibit 49

Agreement between Helmut R. Spitzer and AFR,  
dated November 2, 1956 - Plaintiff's Exhibit 108.

26. In or about August 1956, the Industrial  
Division of AFR commenced operating and began selling indus-



## STIPULATED FACTS

trial foam rubber to manufacturers of foam rubber products for use in such manufacturing. At or about the end of 1956, by agreement of all of the officers and directors of AFR, Buchman was placed in charge of the Industrial Division of AFR and Pathy in charge of the Retail Division, and these arrangements continued until May 17, 1957.

27. At or about the end of 1956, Gerard Lafond was engaged as Assistant Plant Manager of AFR, to work under Felix Buskey.

28. In or about August 1956, AFR entered into a factoring agreement with Hubschman & Co. Factors, under which the said factors would purchase such accounts receivable of AFR as they determined on a non-recourse basis.

C. Facts Relating to the May 17,  
1957 Severance of Buchman and A.  
Sander Buchman from AFR.

29. On or about February 1, 1957, Buchman wrote to Pathy a letter marked Defendants' Exhibit T-14 on the pre-trial depositions. Pathy replied by a letter dated February 4, 1957, a true copy of which is in a folder marked Plaintiff's Exhibit 95 on the pre-trial depositions.

30. On May 17, 1957, the Series A and Series B debentures of AFR and the Burlington Holding debentures were owned, of record, by the parties as follows:

## STIPULATED FACTS

<u>Name of Holder</u>	<u>American Foam Series A Debenture Due May 1, 1960</u>	<u>American Foam Series B Debenture Due May 1, 1965</u>	<u>Burlington Debenture Due April 1, 1960</u>
Samuel Buchman	\$48,000	\$64,000	\$12,000
Marie Louise de Montmollin	63,000	79,000	15,000
Alexander F. Pathy	-0-	80,000	-0-

31. On May 17, 1957, Buchman sold<sup>d</sup> his entire stock interest in AFR and Burlington Holding to the individual defendants and resigned as an officer and director of AFR.

32. At the time of said sale, two agreements dated May 17, 1957 were made, one of them between Buchman and A. Sander Buchman as sellers and the individual defendants as buyers (hereinafter referred to as the "May 17, 1957 agreement") and the other between Buchman and AFR (hereinafter referred to as the "severance agreement").

33. The document marked as Defendants' Exhibit T-2 on the pre-trial depositions is a duplicate original of the May 17, 1957 agreement.

34. The document marked as Defendants' Exhibit T-1 on the pre-trial depositions is a duplicate original of the severance agreement.

35. Buchman continued to retain his Series A debentures of AFR aggregating \$48,000, Series B debentures



## STIPULATED FACTS

of AFR aggregating \$64,000, Burlington Holding debentures aggregating \$12,000 and a 5% promissory note of AFR in the sum of \$25,000.

36. (a) Plaintiffs claim that the individual defendants violated the subordination provisions of paragraph SIXTH of the buy-sell agreement and that they thereby are indebted to plaintiffs in the principal amount of \$64,000. This claim is disputed by the individual defendants.

(b) The individual defendants made all of the other payments provided for in the buy-sell agreement on or about the dates provided therefor.

37. AFR made all of the payments to be made by it under the severance agreement, on or about the dates provided therefor.

38. Buchman was paid the interest and principal amount of his Series AFR debentures and his Burlington Holding debentures as well as the \$25,000 note on or about their due dates. He was paid until and including August 1, 1960, as it fell due, interest on his Series B debentures aggregating \$64,000 but was not paid any of their principal nor any interest thereon falling due after August 1, 1960.

D. Events and Transactions After  
May 17, 1957.

## STIPULATED FACTS

39. On or about June 1, 1957, the defendant Alexander F. Pathy sold his Series B debentures to the defendant de Montmollin for \$80,000 and received such amount from her, in payment therefor.

40. In or about April or May 1953, the individual defendants in their capacities as officers, directors and stockholders of AFR caused the certificate of incorporation of AFR to be amended so as to provide for 3,500 shares of 5% cumulative preferred stock of the par value of \$100 each, and thereafter in or about May 1953, the defendant de Montmollin surrendered to AFR debentures and notes in the total face amount of \$291,000, which she owned, and received in exchange therefor 2,910 shares of preferred stock. In or about December 1959, the defendant de Montmollin surrendered additional debentures and notes in the total face amount of \$31,000, which she owned, and received in exchange therefor 310 shares of preferred stock.

41. In response to the request of Howard Herbert, he and Pathy received the reports from the following Industrial Division salesmen, bearing the following dates, true and correct copies of which are marked as follows as exhibits on the pre-trial depositions:

Donald B. Parker	Nov. 10, 1957	Plaintiff's 65
Irving Mirsky	Undated	Plaintiff's 66
Helmut R. Spitzer	Nov. 11, 1957	Plaintiff's 67



## STIPULATED FACTS

42. On or about January 1, 1958, Angelo Cecchi began working for AFR to assist in administrative and accounting matters. He was at all times so employed by AFR between January 1, 1958 and January 30, 1961.

43. In or about November 1957, AFR engaged as an Industrial Division salesman, to work part time, William Stein, of Chicago, Illinois.

44. Prior to May 17, 1957, Felix Buskey worked closely with and under Buchman. On May 17, 1957, Felix Buskey had charge of AFR's foam rubber manufacturing plant and was in charge of sales of the Industrial Division.

45. A meeting of the Industrial Division salesman of AFR was held at the office of AFR, in the Empire State Building, New York, N.Y., on March 5, 1958.

46. On February 13, 1958, Gerald Lafond tendered his written resignation from his position with AFR. He did resign and terminate his employment prior to the end of February 1958.

47. In 1958 Louis Levy instituted arbitration proceedings against AFR and its subsidiary, Mirofoam Industrial Sales, Inc. before the American Arbitration Association, Case C 13403 PHI-C-53-58 to recover the drawing account claimed to be due and owing to him under an agreement entered into between him and AFR dated July 30, 1956 (Plain-

## STIPULATED FACTS

tiffs: Exhibit 43). Pre-trial Exhibits 1, 2 and 3 are accurate copies of briefs submitted at the hearing in the said arbitration proceeding and the minutes of the testimony taken thereat.

48. The position of Louis Levy in such arbitration proceeding was that he had not resigned on March, 30, 1958 and that the letter received by him from AFR dated April 1, 1958 constituted a notice of termination of his employment and did not become effective until thirty days thereafter.

49. Pre-trial Exhibit 4 is an accurate copy of the award of the arbitrator rendered in the said arbitration proceeding.

50. In 1958 Irving Mirsky instituted arbitration proceedings against Mirafoam Industrial Sales, Inc., a wholly owned subsidiary of AFR before the American Arbitration Association, Case 13403-PHI-C-5-58 to recover the drawing account claimed to be due and owing to him under an agreement dated December 3, 1956 (Plaintiffs: Exhibit 47). Pre-trial Exhibit 5 is an accurate copy of the minutes of the testimony taken thereat.



## STIPULATED FACTS

51. The position of Irving Hirsch in such arbitration proceeding was that he had not resigned on March 30, 1958 and that the letter received by him from Hirafoam Industrial Sales, Inc. dated April 1, 1958 constituted a notice of termination of his employment and did not become effective until sixty days thereafter.

52. Pre-trial Exhibit 6 is an accurate copy of the award of the arbitrator rendered in the said arbitration proceeding.

E. Miscellaneous Facts.

53. In or about September 1965, Felix Bushey, died.

54. On January 24, 1961, commencing at 10:30 a.m., a hearing was held before the Honorable Robert P. Stephenson, Referee in Bankruptcy, at the United States Court House, Foley Square, New York, N.Y., pursuant to Rule XI-4 in the matter of the arrangement proceedings of AFR. The minutes of said meeting, a copy of which is marked Plaintiff's Exhibit 207 on the pre-trial depositions, correctly set forth the appearances and proceedings at the said meeting.

55. On February 21, 1961, commencing at 10:30 a.m., the initial meeting of creditors of AFR was held before the Honorable Robert P. Stephenson, Referee in Bankruptcy, at

STATEMENT OF ISSUES.

VIII. The issues to be tried are formulated by the Court (with the consent and agreement of the parties) as follows:

- a) Did the individual defendants by their actions and conduct breach the subordination provisions of the May 17, 1957 agreement entered into by them with Samuel Buchman?
- b) Did Buchman conspire with important employees of American Foam Rubber Corporation or its subsidiaries to injure or destroy American Foam Rubber Corporation or the value of the individual defendants' investments therein?
- c) If he did, were acts committed in furtherance of such conspiracy?
- d) What is the pecuniary amount of the damage done to American Foam Rubber Corporation by Buchman's conspiracy?
- e) What is the pecuniary amount of the damage done to the individual defendants by Buchman's conspiracy?
- f) Should Ackman recover punitive damage



## JURY VERDICT ON DEFENDANTS' COUNTERCLAIM.

BUCHMAN v. AFR

Did Buchman conspire with important employees of American Foam Rubber Corporation or its subsidiaries to injure or destroy American Foam Rubber Corporation or the value of the individual defendants' investments therein, and were acts committed in furtherance of such conspiracy, and were the defendants damaged by such acts?

☒ YES☐ NO

EXCERPTS FROM TRANSCRIPT.  
TESTIMONY OF ALEXANDER PATHY.

A L E X A N D E R . P . P A T H Y, one of the  
defendants, called as a witness by the  
defendants, being first duly sworn,  
testified as follows:

THE COURT: The last time you testified,  
Mr. Pathy, I had you on my right, now I have you  
on my left, and let us see if we can make it much  
more brief when you are on my left.

Come on, Mr. Sive, right to the heart of  
it.

MR. SIVE: Yes, sir.

DIRECT EXAMINATION BY MR. SIVE:

Q Mr. Pathy, what office did you occupy  
with AFR at or about the end of 1956?

A Executive vice-president.

Q Do you recall offhand the approximate  
capital of the company in early 1956?

A A little over \$400,000.

Q Do you recall the capital of the company  
at or about the end of August, 1956, approximately?

A Not much more. I don't remember the  
answer.

Q Do you recall the approximate capital  
of the company in May, 1957?



fppl4

Pathy-direct

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A It was still less than \$500,000.

Q And at the end of 1957, do you know?

A Over 600,000.

Q What was the situation of the company with respect to its capital needs at the end of 1957?

A The company needed much greater capital than it had because its sales doubled or about in 1957 as compared to 1956.

Q What was the reason essentially for the sales doubling in 1957 as compared with 1956?

A The building of the new industrial plant and division.

Q What was the situation of the company at or about the end of 1957 with respect to the credit rating or ratings of the company?

A The company had no rating.

Q Did the company -- that is the management of the company -- decide in late 1957 or thereabouts to do anything about the capital of the company and the credit rating?

A Yes.

Q What did it decide to do with respect to the capital?

fppl5

Pathy-direct

A To increase the capital and increasing the capital, to get the credit rating, the highest it could get, and thereby also get the highest borrowing capacity for the company.

Q You referred to borrowing capacity. What institution was the lender supplying the company funds in 1957?

A The Pennsylvania Bank.

Q What was the type or description, just the very general description, of the kind of credit which the bank granted to the company during 1957?

A A term loan of \$400,000, and up to the end of 1957, a revolving loan of \$100,000.



Q And is the term loan to which you referred the loan provided for by the term loan agreement, a copy of which is Exhibit EN?

A Yes.

Q And is it correct that that term loan was secured by the pledge or mortgaging of the property as provided in Exhibit EN?

A Yes.

Q Now, was the revolving credit secured at all?

A No.

Q And is it correct that there were two separate types of loans in '57?

A Yes.

Q Prior to June 1, '58, or at or about the end of '57 did the company have any business or any dealings with Dun & Bradstreet?

A No.

Q Did the company do anything with respect to Dun & Bradstreet in 1958?

A Yes.

Q Could you describe very briefly what it attempted to do?

A It attempted to get a rating; the first

condition to get the rating was to communicate to Dun & Bradstreet the last statement and the previous statements of the company.

The company, by Mr. Buchman, who was the company's president, never disclosed any of its operating statements.

Q Now I show to you the exhibit marked EZ for identification and ask you --

MR. SIVE: Let me withdraw that, your Honor.

THE COURT: I would like to have the witness finish the Dun & Bradstreet. He said one of the conditions was, and he gave us that. What else, if anything, in order to get a credit rating in '58 with Dun & Bradstreet, what did you understand had to be performed?

THE WITNESS: The basic condition was to communicate a statement and depending on what that statement would show, there would be a rating.

THE COURT: All right.

Q Now, what was your understanding as to what the statement would have to show to secure the rating that you sought?

A The capital of the company had to be



over a million dollars and there were other conditions in order to get that kind of rating.

THE COURT: You see that is just what I am trying to get you to tell us. What were the conditions?

THE WITNESS: The other conditions were the mode of payment of the company's invoices. That was a very important condition. They had their own way of appraising the management, and those were the basic conditions.

THE COURT: All right.

Q Well, was one of the conditions, as you understood it, to secure the rating, a capital of a million?

A Yes, for the AAL rating.

THE COURT: That is what he testified.

MR. SIVE: Your Honor, might I at this point point out that one of the documents marked for identification is the Key To Rating which is just the table which your Honor, I respectfully ask, examine in connection with this testimony.

THE COURT: Yes, yes. I understand why you had those documents marked in evidence before Mr. Pathy took the stand. I understand.

Q Mr. Pathy, was the capital of the company increased in 1958?

A Yes.

Q Was it increased to over a million?

A Yes.

Q How was that increased effected?

THE COURT: How was it accomplished, yes.

Q Stating it very briefly, if you can.

X A To the company's own capital and retained earnings were added about \$300,000 as a result of the exchange of long-term debts which were the debentures, plus \$120,000, which were donated by the then-stockholders in form of the stock of Burlington Holding, which was the owner of the real estate. The two amounts, 300 and 120, 420 added to the then-existing capital of AFR, brought the total over \$1,000,000, plus X-

MR. SIVE: Your Honor, if I may just point out, that statements heretofore submitted deal with the same matter, which is the testimony now.

THE COURT: So I gather.

Q Now, sir, you referred to the donation of Burlington stock. Prior to the donation who owned the Burlington shares?



A The individual stockholders personally.  
It was not a subsidiary of AFR.

Q And were some of those shares part  
of the subject of sale under the Buy-Sell  
Agreement which is the subject of this action?

A Yes.

Q How was the amount of \$120,000, which  
was added to the capital by virtue of that donation  
of the Burlington shares to the company, arrived at?

A In order to acquire one-third of Burlington  
Holding stock, we paid Mr. Buchman \$40,000 cash.  
Since each of the two of the stockholders owned  
one-third, donating all of the stock of Burlington  
was equivalent to a donation of \$120,000.

Q And was that done by the accountants  
of the company in the statements thereafter  
rendered by them?

A Yes.

MR. SIVE: Your Honor, at this time I  
will simply, I think, call your Honor's attention,  
or reread, whichever your Honor wishes, the  
one paragraph of stipulated facts, paragraph 40,  
in the pre-trial order. If it would help  
your Honor, I will reread it at this time.

THE COURT: Yes.

MR. SIVE: "In or about April or May of 1958, the individual defendants in their capacities as officers, directors and stockholders of AFR, caused the certificate of incorporation of AFR to be amended so as to provide for 3500 shares of 5 per cent cumulative preferred stock of the par value of \$100 each and thereafter, in or about May, 1958, the defendant, de Montmollin, surrendered to AFR debentures and notes in the total face amount of \$291,000 which she owned and received in exchange therefor 2910 shares of preferred stock. In or about December, 1959, de Montmollin surrendered additional debentures and notes in the total face amount of \$31,000 which she owned and received in exchange therefor 310 shares of preferred stock."

BY MR. SIVE:

Q Now, Mr. Pathy, you heard me refer to Mrs. de Montmollin surrendering additional debentures and notes at the end of 1959, in or about December, in the amount of \$31,000. Did the company at or about that time issue any



additional shares of preferred stock?

A Yes.

Q To whom?

A To a company in which I was controlling  
at that time.

Q What is the name of the company?

A General Industrial Supply Corporation.

Q In what amount?

A For \$120,000.

Q And in what form was that paid into the  
company?

A Cash.

MR. SIVE: Your Honor, could I ask that  
at this point we simply stipulate, in lieu of  
putting in evidence another fat book, that the  
stubs of the certificates of preferred stock issued  
to General Industrial Supply Corp. at or about  
December 31, '59, in connection with the purchase  
of those shares by that company at or about that  
time appear in the preferred stock certificate  
book which Mr. Greenwald has let me take here.

THE COURT: All right. Mr. Whyman?

MR. WHYMAN: All right.

MR. SIVE: It is so stipulated.

THE COURT: Will you read the exact wording on that stub?

MR. SIVE: Yes, there are stubs --

THE COURT: No, on that particular stub.

MR. SIVE: Yes, your Honor.

Well, there are several, but on stub bearing No. P9, dated December 31, '59, it states -- and I am combining the printing and the longhand -- "Certificate No. P9, 4100 shares issued to General Industrial Supply Corp., 305 Madison Avenue, New York 17, NY, dated December 31, 1959. From whom transferred: Original issue."

Similar stubs appear and are marked P-10, P-11, P-12, 13, 14, 15, 16, 17, 18, 19, 20, all to General Industrial Supply Corp.

THE COURT: With the same legend?

MR. SIVE: With the same legend, except for the number of the stub.

THE COURT: Yes.

MR. SIVE: Now, I will also ask that it be stipulated that there are three additional stubs, Nos. 21 through 23, setting forth the issuance of shares of preferred stock to Mrs.



de Montmollin, and bearing the same dates.

(Pause.)

MR. SIVE: It is so stipulated, your Honor, by Mr. Whyman, myself, and these need not be marked in evidence.

THE COURT: Very well.

BY MR. SIVE:

Q What was the approximate capital of the company at or about the beginning of December, 1959?

A About \$900,000.

Q What was the purpose of the purchase of additional shares of preferred stock by General Industrial and by Mrs. de Montmollin?

A To bring the capital again over \$1,000,000 and thereby retain the AAL rating of Dun & Bradstreet.

Q Was there any change of the source of the company's financing in 1959?

A Yes.

Q Describe briefly who substituted or who succeeded whom?

A Walter E. Heller & Co. substituted the Pennsylvania Bank and Irving Trust.

MR. WHYMAN: May I have that answer read back, please?

THE COURT: Yes, Mr. Court Reporter, would you please read the answer.

(Answer read.)

MR. SIVE: I think the witness means "substituted for" the Pennsylvania Bank.

THE COURT: Did you mean that?

THE WITNESS: Yes.

THE COURT: All right.

MR. SIVE: May I at this time, your Honor, point out facts which I think are not in dispute, and this is to save testimony, that on December 3rd the underlying loan agreement, a copy of which is FA, was executed by and between the company, and its subsidiaries, and Heller, and Exhibit FB and FC, the Ruben and Weaver memoranda respectively, set forth certain details of the opening of the loans and the beginning of the loan and borrowing relationship.



BY MR. SIVE:

Q Was there any communication between you and Heller in or about December 1959 with respect to the sale by the company of additional shares of preferred stock?

A Yes.

Q What, in substance, was told to Heller and by whom?

A I told to Mr. Peter Heller that we --

MR. WHYMAN: Just a minute. I am going to object to it, if the Court please, on the ground that it purports to be an extra judicial statement which would be hearsay as far as we are concerned as to what was told to Mr. Heller.

MR. SIVE: I will explain, your Honor, why it is not hearsay.

THE COURT: All right.

MR. SIVE: Hearsay is proof of facts alleged in a statement by proving the statement made out of court. In this case we are not proving the fact alleged in the statement. We are proving the fact of the making of the statement which is significant because it sets forth what was the purpose of selling additional shares of preferred stock,

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and it ties directly into the Weaver and Ruben memoranda which paraphrase and state that they were told what this witness is now being asked to say he said.

MR. WHYMAN: I will accept Mr. Sive's statement that he is not attempting to offer hearsay testimony, but he simply trying to show that a statement was made. As to that I will not object. But as to the content of the statement, I will object to it. So subject to that --

MR. SIVE: I think that disposes of the objection. By this I simply want to prove that the statement was made.

THE COURT: All right, proceed.

MR. SIVE: And the balance of the proof will come otherwise.

THE COURT: All right.

BY MR. SIVE:

Q Could you, Mr. Pathy, tell us what if anything you said at or about when to Heller with respect to the issuance of additional shares of preferred stock?

MR. WHYMAN: That is the objection I raised.



THE COURT: Yes, it is. That is exactly the objection he raised.

MR. SIVE: Your Honor, I submit that the statement of what was said proves what was said and proves the fact of that having been said but does not prove the truth of what was said.

THE COURT: Objection overruled. I will take it.

A I informed Heller that we decided to increase the capital of AFR to over \$1 million so as to retain our AA-1 rating with Dun & Bradstreet.

Q Other than the exchange of debentures for shares of 300,000, the donation of Burlington stock for 120,000 and the sale and purchase of additional shares of preferred stock at the end of December '59, were any other loans, advances or investments made by you or Mrs. de Montmollin between March '58 and December 1960?

A Yes.

Q Could you describe very briefly the approximate amount, the nature of each such loan or advance or investment and the approximate date, if you can, without refreshing your recollection?

A In December of 1959 Mrs. de Montmollin

exchanged a note of \$25,000 for preferred shares.

In July of 1960, General Industrial Advanced AFR first 5,000, then another \$25,000.

In August or September of 1960 I caused two companies in which I had family contacts to advance to AFR \$40,000, and going back, in April of 1960, Mrs. de Montmollin, who was supposed to receive \$15,000 on her A bond Burlington debentures did not receive \$15,000 on those bonds, but loaned those \$15,000 to AFR.

Q What was the approximate total of investments and loans by you and the other individual defendants or companies in which you had an interest between January 1, '58 and the end of 1960?

A About \$650,000.

Q And of that total, approximately what amount was on account of purchases of preferred stock?

A Yes.

Q Approximately what amount of that total?

A Approximately more than half.

Q Well, was the total amount 300 plus 125 issued by General Industrial, plus 30 or thereabouts purchased by Mrs. de Montmollin at the end of '59?



A That's right, about 460,000.

Q Has any dividend ever been received by you or any other individual defendant on those shares of stock?

A No.

Q Was the payment of any dividend on such shares of stock ever suggested at any meeting of the Board of Directors or stockholders of the company?

A No.

Q Was it ever suggested at any time otherwise?

A No.

Q Did Mrs. de Montmollin or any other holder of the preferred shares ever ask for any dividend?

A No.

Q If I ask you the same series of questions with respect to sale to the company of such shares of preferred stock, would the answers be the same?

A Yes.

Q Was the exchange transaction part of a plan to obtain cash from the company?

A No.

Q Was there any such plan to obtain cash

from the company?

A No.

Q Was any such plan ever suggested by anybody?

A No.

Q Did you ever think of any such plan?

A No.

Q Would your answers be the same if instead of cash I ask about cash realizable property?

A Yes.

Q At or about the end of 1957, what amount, if any, was lent to the company by the Pennsylvania Bank under the revolving unsecured credit?

A Nothing. Oh, 19 -- I'm sorry -- yes, nothing.

Q What was the highest amount ever outstanding under any such loans, that is, the unsecured revolving credit line of the bank prior to the end of 1957?

A \$100,000.

Q In January of 1958 did the bank make any unsecured loans?

A No.

Q Did it do so in February?



A No.

Q In March?

A No.

Q In April?

A Yes.

MR. SIVE: May I at this time, your Honor, just point out several entries in Exhibit EU showing that as of September 27, '57, the balance of unsecured credit loans by the bank to the company was zero; on August 27, '57 it was \$80,000. The next entry after September 27, '57, is April 22, '58, which shows 200,000. May 8, '58, the next entry, 300,000 and June 10, '58, 400,000.

Q In or about early 1958, was there any contact between you on behalf of AFR and the Pennsylvania Bank?

A Yes.

Q With whom at the Pennsylvania Bank?

A It was Mr. Leof and Mr. Lauer, both vice-presidents.

Q And essentially what was it about, describe that very briefly?

A I requested the bank for a substantial loan indicating that we intended to increase the

company's capital to over a million dollars, and the bank was first waiting to get our 1957 balance sheet, and then the necessary indications how we are going to go about to raise the capital over the million dollar mark.

Q Did you thereafter send any statements to the bank setting forth the capital?

A Yes.

Q And did the statements that you sent to the bank include copies of the statement, a copy of which is Exhibit EQ? I show to you Exhibit EQ.

A Yes.

THE COURT: Would you announce an interruption of three or four minutes?

THE CLERK: There will be a short recess. All rise.

(Short recess.)



THE COURT: Please proceed.

Q Is it correct, Mr. Pathy, that in early 1958, there was a period of negotiation between AFR and the bank with respect to the bank's application for additional unsecured credit?

A Yes.

Q Approximately when did that negotiation end?

A Early April or end of March.

Q During the course of that negotiation, were there letters back and forth between you and the bank?

A Yes.

Q When I say you, I mean the company, by you or somebody else.

A Yes.

Q And are the copies of letters marked Exhibit ES some of the letters which you have referred to (handing)?

A Yes.

Q What was the interest rate of the credit which the company did secure in or about April 1958?

A If my recollection is right, it was 4-1/2 per cent, and expressed otherwise, 1/2 per cent

over the prime rate.

Q How did that interest rate compare with the interest rate which the company had to pay on prior unsecured loans?

A That was a cheaper rate than what the company paid on prior unsecured loans.

Q Did the company in or about 1958 secure the Dun & Bradstreet rating it sought?

A Yes.

Q Did it maintain that rating?

A Yes.

Q Until when? Did it maintain it through 1958 and 1959?

A Yes.

Q I show to you, Mr. Pathy, the document marked Exhibit 34, the relevant portion of which is marked in brackets, pencil brackets I think by Mr. Whyman, and ask you do you recall being shown that document during the taking of your deposition in this proceeding?

A I don't remember.

Q Would the minutes of the testimony refresh your recollection?

A Yes.



Q Will you please look at the record of the minutes of your testimony on the deposition and tell me if it is correct that you did look at this exhibit or it was shown to you during the course of the deposition.

THE COURT: And by "this exhibit" you are referring to?

MR. SIVE: The exhibit marked here 34 and marked on the deposition 194. The witness is looking at page 946 of his deposition.

THE COURT: All right, give him a chance to examine it.

THE WITNESS: Yes.

MR. WHYMAN: I object to --

THE COURT: Have you examined it?

THE WITNESS: Yes.

MR. SIVE: He answered the question.

Do you object to the question?

MR. WHYMAN: No.

MR. SIVE: Then let us have the answer.

Q The answer was?

A Yes.

MR. WHYMAN: If the Court please,

Mr. Sive referred to a different marking on this exhibit, namely, the marking 34. That is -- withdrawn.

Q But you did see the document?

A Yes.

Q At the time that you saw that document, what was your understanding as to the word "payment" referring to the phrase "arising from payment of bonds"?

MR. WHYMAN: I am going to object to that, if the Court please, as to what his understanding was at the time he saw the document.

THE COURT: Yes, which in turn caused him to testify in some fashion.

Objection overruled.

A Legal discharge.

THE COURT: Legal discharge?

THE WITNESS: Of the obligation.

THE COURT: Of the obligation.

Q What obligation?

A Of the payment of the bond.

Q I show to you, sir, Exhibit 33, which is the minutes of the Board of Directors meeting of AFR held on December 2, 1959. What was the main



event happening to the company at or about  
December 2, 1959?

A The changeover from the Pennsylvania  
Bank to the Heller outfit. In December 1959?

Q Yes.

A The change of our borrowing source.

Q Now, sir, I show to you a page which is  
unnumbered of the minutes of that meeting --

THE COURT: A page from what exhibit?

MR. SIVE: Of Exhibit 33.

THE COURT: It appears after what numbered  
page?

MR. SIVE: None of the pages are  
numbered, your Honor, but it is the fifth unnumbered  
page in order.

THE COURT: All right.

Q And I show to you the last paragraph beginning  
with the word "resolved" and continuing over to the  
sixth unnumbered page. Please read that and then  
I will ask you a question.

A What is the question?

Q Do you remember who prepared those  
minutes or dictated them?

A I don't remember.

Q Did you see the minutes at any time?

A Yes.

Q And what was your understanding at the time you saw them of the use of the term or the meaning of the term "authorized to issue shares of the 5 per cent cumulative preferred stock of the corporation in payment of outstanding indebtedness of the corporation"?

A Again, legal discharge.

Q Did there come a time at the end of 1960 or thereabouts when the company filed an arrangement petition?

A In 1961.

Q In January of 1961?

A Yes.

Q And was there thereafter a hearing?

A Yes.

Q Were you present at the hearing?

A Yes.

Q Would you look, please, at page 27 of Exhibit 38, that exhibit being the minutes of the hearing pursuant to Rule XI-4 in the arrangement proceeding of AFR. Could you please read just that page and then I will ask you a question



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about it (handing).

A Yes.

Q Do you see the point where the witness, yourself, is quoted, and shortly below the middle of the page there are the words by you "Since we created these preferred shares --"

Do you recall at that point the Referee asking you that question that appears after that?

A Yes.

Q And what was your understanding then of the meaning of the words "Paid to the stockholders"?

A The same, discharge -- a legal discharge of an obligation.

Q Now, sir, it is correct, is it not, that after the Buy-Sell Agreement between you and Buchman, you sold your debentures to Mrs. de Montmollin?

A Yes.

Q And she paid you \$80,000?

A Yes.

Q Why did you sell them to her?

A For the reason that I just bought Mr. Buchman's common stock and I have to pay him cash and I didn't have sufficient cash to pay for it, so what I sold for I paid over to Mr. Buchman.



Q That is the cash you received from Mrs. de Montmollin?

A The cash I received, that's right.

X Q You heard testimony here about the loan to officer -- I think that is the term -- of \$15,000 set forth on a report of Edward Isaacs, a copy of which has been marked in evidence by the plaintiffs, specifically Exhibit 35.

Do you see the entry on Exhibit 35 entitled "Loan Payable Officer, \$15,000"?

A Yes.

Q Who is that officer?

A Mrs. de Montmollin.

Q And how did the \$15,000 entry come about?

A She had Burlington Holding bonds or debentures which matured in April of 1960. By that time Burlington was a subsidiary of American Foam. The same amount of \$150,000 which were supposed to be paid to her but were not paid, were loaned by her to AFR, and therefore it became a loan of an officer to AFR.

Q Was any amount ever paid to Mrs. de Montmollin on that loan?

A No.

Q Was any cash or any property ever paid or transferred to Mrs. de Montmollin on account of that \$15,000 Burlington debenture?

A No.

Q Was any cash realizable property ever paid to her for that?

A No.

Q Did she ever ask for it?

A No.

Q Did she ever mention it to you?

A No.

Q Did the company ever consider paying any cash or cash realizable property to her for that \$15,000 debenture?

A No.

Q Is that \$15,000 indebtedness owed by the company now?

A Yes. X

Q And is the \$15,000 indebtedness set forth in a claim filed in the bankruptcy proceedings?

A Yes.

Q Who is the maker and owner of that claim?

A I don't remember the name, but that was handled by Mr. Sidney Krauss.



Q And Mr. Sidney Krauss was the bankruptcy attorney who advised the company at the time of the filing of the Chapter XI petition, is that right?

A That's right.

THE COURT: I think, Mr. Sive, this might be as good a time as any to adjourn for the day.

I must say to both of you that you have been most helpful. I am not unmindful of the great amount of work that must have gone into your getting together on so many of these documents. Your courtesy to one another and to me is appreciated. I hope that it will be sustained throughout the balance of the proceeding.

Gentlemen, thank you again, and we start promptly at 10 o'clock tomorrow morning.

(Adjourned to December 4, 1968, at  
10.00 a.m.)

\* \* \*

you down.

MR. SIVE: I will probably conclude with this witness. I may have just some deposition reading, very briefly.

THE COURT: You are doing all you can, both of you, and we will just have to go over. You didn't know I was going to have this meeting.

REDIRECT EXAMINATION BY MR. SIVE:

X Q Mr. Pathy, referring to the recent series of questions by Mr. Whyman, you used the phrase, and I tried to take it down correctly, but you correct me if I did not do it precisely, that if and when at any time the corporation would pay the debentures -- and now I am paraphrasing, and again, you correct me if I am wrong -- it would have to pay Buchman first before paying the other debenture holders.

A Yes.

Q Now, when you spoke of "paid the debentures," with what were you speaking of, payment with what?

A Well, the payment here is what I, and I believe everybody ---

THE COURT: No, please, don't do that now.

A Payment with assets of the company, assets of the corporation, coming out of the corporation.



THE COURT: All right.

A This is payment.

Q And was that your understanding of the word "payment" when you testified to that two minutes ago?

A Yes, that was my understanding.

Q Was that your understanding of the word "payment" and "paid" and "pay" as used in the subordination agreement at the time it was drafted and executed?

A It was.

Q Has that been your understanding at all times since?

A Yes.

Q And was it on the basis of that understanding that you executed the agreement?

A Yes. X

Q Was any payment out of the assets of the company ever made on any of the debentures?

A No.

Q I should ask, ever made on any of the debentures held by you or Mrs. de Montmollin.

A No.

Q At the time of the exchange, who owned all of the stock? Just give me the names of the persons.

A Common stock?

Q All of the stock. State the names of all of the stockholders immediately prior to the exchange.

A Mr. Buchman --

Q No, immediately prior to the exchange.

A Oh, the exchange.

Q Yes.

A Mrs. de Montmollin, my wife and myself.

Q Immediately after the exchange who owned all of the stock?

A Again, common stock, the same.

Q Well, is it correct that immediately before the exchange and immediately after the exchange all of the stock was owned by yourself, your wife and Mrs. de Montmollin?

A That is correct.

Q And is it correct that all of the stock, the holders of all of the stock owned immediately before the exchange and immediately after the exchange, all of the net worth of the company?

A Yes.

THE COURT: You yourself, Mr. Sive, found objection to Mr. Whyman when he spoke of "all the stock."



Now, I should think that that might very well lead a witness to believe that what you are talking about is owning common stock, or are you talking about preferred stock? What stock?

Why don't you define exactly what you want to say? What stock?

Q Well, is it correct, sir, that at the time of --

A It is still true that all three of us owned all the stock.

Q At the moment preceding the exchange or immediately before the exchange and between that time and the time previous, right after the execution of the stock deal, name the persons who together owned all of the stock.

A Mrs. de Montmollin, my wife and myself.

Q Name the persons who together owned all of the stock of all classes immediately after the exchange?

A The same.

THE COURT: That is the first time you said "all classes."

A The same.

THE COURT: All right.

Q Was any payment of any asset made to anybody in and by the exchange?

A No.

Q Was any payment of any asset made by the company in and by the sale by you of debentures to Mrs. de Montmollin?

A No.

Q Was any payment of any asset of the company made to anybody in and by the bookkeeping entries which you have described with respect to the Burlington debenture held by Mrs. de Montmollin and the loan to officer by the company in or about April, 1960?

A No.

X Q In Paragraph 6(a) of the stock sale agreement, Exhibit 40, the subordination agreement, the word "paid" appears and the word "paid" appears.

What was your understanding at the time of the execution of the agreement as to what persons were referred to by those two verbs?

Do you want to look at the agreement?

A Yes, please. Will you show me where?

(Handed)

A The two persons, one is the corporation and the other is the holder.



Q And of the two who would be doing the paying?

A The corporation.

Q And was that your understanding during the drafting of the agreement?

A Yes.

Q Was it your understanding at the time of execution of the agreement?

A Yes.

Q And at all times since?

A Yes. X

MR. SIVE: I think I can confer for a moment with Mr. Whyman and save time. Give me a moment?

THE COURT: Surely, I will give you a couple of minutes.

(Pause)

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FIRST NATIONAL BANK OF HOLLYWOOD,  
et al.,

vs.

60 Civ 2328

AMERICAN FOAM RUBBER CORPORATION,  
et al.

New York, December 5, 1968;  
11.00 o'clock a.m.

Trial resumed.

- -

A L E X A N D E R F. P A T H Y, resumed.

REDIRECT EXAMINATION CONTINUED BY MR. SIVE:

THE COURT: Please proceed.

MR. SIVE: I will go very briefly  
and conclude the redirect examination of the  
witness.

THE COURT: Certainly.

Q Mr. Pathy, I show to you Exhibits EP  
and EQ concerning which you were asked some  
questions on the cross-examination, and I  
direct your attention, if I may, to the  
capital accounts set forth thereon. This  
may be somewhat repetitive of what I asked  
you on your direct examination, but I will  
ask you to bear with me. What was the  
capital of the company as at the earlier  
statement, the one I believe as at February 1,



1958?

A February 2, 1958, was before the exchange.

Q Yes, what was the capital as of that date, the amount?

A The capital at that date was \$476,242 and composed of two items: Capital stock issued, which was the common stock, for \$287,330 and surplus \$188,912.

Q That surplus was an earned surplus; is that right?

A Earned surplus.

Q What was the amount of the capital as at the date of the later statement, EQ?

A EQ, the later statement, after exchange, total capital was \$1,021,248, composed of the amount of common stock which varied by \$1000, \$278,330; the preferred stock which came from the exchange, \$300,000, Burlington Holding, the donation which amounted to \$120,000 and earned surplus, which at that time was \$322,918. So the only difference in capital, which was not added between these two statements, is the increase in the earned surplus due to

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the fact that in the first statement the earned surplus as of December 31, 1957, had not yet been added. Otherwise the two statements are completely identical before and after the exchange.



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OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969.

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

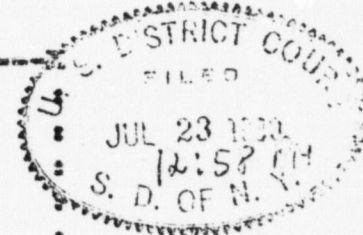
FIRST NATIONAL BANK OF HOLLYWOOD,  
DOROTHY BUCHAN and A. SANDER  
BUCHAN, as Executors of SAMUEL  
BUCHAN, Deceased,

Plaintiffs,

-against-

AMERICAN FORM RUBBER CORPORATION,  
MILTON R. ACHORN, as Trustee of AFR,  
MARIE LOUISE DEMONTHOLAIN, ALLEMANDE  
P. PATRY and SUZANNE M. PATRY,

Defendants.



60 Civ. 2328

Opinion  
# 36027

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OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

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IRVING BEN COOPER, D. J.

American Foam Rubber Corporation (hereinafter AFR) was organized in 1950 under the laws of the State of New York. From the time of organization until May 17, 1957, Samuel Buchman served as its president and operating head. On the latter date an agreement (hereinafter the Buy-Sell Agreement) was entered into between Buchman and the individual defendants, Alexander F. Pathy (hereinafter Pathy), Suzanne M. Pathy (Pathy's wife) and Mario Louise de Montmollin (also a relative), under the terms of which Buchman sold his entire stock interest in AFR and Burlington Holding Corporation (hereinafter Burlington)<sup>1</sup> to the individual defendants and

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1. Burlington became a wholly-owned subsidiary of AFR on April 30, 1958.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

resigned as an officer and director of AFR.<sup>2</sup> AFR's business was thereafter conducted by Pathy as president and the other individual defendants as officers and directors.

To induce Buchman to sell his capital stock, Pathy and deMontmollin agreed to subordinate certain debentures of the corporations then held by them to the rights of holders of specified debentures then held by Buchman. The terms of this subordination are embodied in subparagraph A of the SIXTH paragraph of the Buy-Sell Agreement:

The parties named below hold five (5%) percent registered debentures issued by American Foam or Burlington in the following respective amounts:

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2. Under the terms of the Buy-Sell Agreement, Buchman's son, A. Sander Buchman, also sold his entire stock interest in AFR to the individual defendants.

OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

	AMERICAN FOAM SERIES A DEBEN- TURE	AMERICAN FOAM SERIES B DEBEN- TURE	BURLINGTON DEBENTURE
<u>NAME OF HOLDER</u>	<u>DUE MAY 1, 1960</u>	<u>DUE MAY 1, 1965<sup>(3)</sup></u>	<u>DUE APRIL 1, 1960</u>
SAMUEL BUCHMAN	\$48,000	\$64,000	\$12,000
MARIE LOUISE de MONTMOLLIN	63,000	79,000	15,000
ALEXANDER F. PATHY	-0-	80,000	-0-

To induce Samuel Buchman to sell his capital stock hereunder, Maria Louise deMontmollin and Alexander F. Pathy hereby agree with respect to the debentures of each of said corporations that the rights of any holder (including her or him) of the debentures thereof now held by her or him and referred to above, be subordinated to the rights of any holder or holders of the debentures thereof now held by Samuel Buchman (including him) as to the payment of interest and principal. No claim for interest under the debentures so subordinated shall be made unless all interest payable on the debentures now held by Samuel Buchman shall have been paid in full, and no claim for principal under any of the debentures so subordinated shall be made unless the entire principal of all the debentures now held by Samuel Buchman shall have been paid in full.

- 
3. "Due May 1, 1965" should read "Due August 1, 1965."  
See Exhibit 37 and the trial transcript at page 15.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

If for any reason, either corporation shall pay interest or principal on said debentures to any of the Buyers, or to any person deriving title to the debentures of said corporation from any of the Buyers, and said payment shall be made without first satisfying the priority to which the holder or holders of Samuel Buchman's debentures are entitled by reason of the foregoing provisions, the amount or amounts of the payment so made to the Buyer (or to the person deriving title from her or him) shall be promptly paid by such Buyer to said holder or holders of Samuel Buchman's debentures. Any payment made on account of principal shall be endorsed on said debentures, which shall be submitted to the payor for that purposes.

On June 1, 1957, Pathy sold his Series B AFR debentures to deMontmollin for \$80,000 and received such amount from her in payment thereof. (PTO 39.)<sup>4</sup>

In April 1958, "the individual defendants in their capacities as officers, directors and stockholders of AFR caused the certificate of incorporation of AFR to be amended so as to provide for 3,500 shares of 5%

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4. "PTO" followed by a number refers to paragraphs of the Pre-Trial Order dated March 15, 1968.

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cumulative preferred stock of the par value of \$100 each ...." (PTO 40.) At a special meeting of AFR's Board of Directors held on April 23, 1958, it was resolved that shares of the new 5% cumulative preferred stock be issued in exchange for AFR Series A and Series B debentures and 5% promissory notes surrendered to the corporation at the rate of one share of stock for each \$100 face amount of said debentures and notes. (EX.FD.)<sup>5</sup>

In May 1958, deMontmollin surrendered AFR debentures and notes owned by her in the aggregate face amount of \$291,000 to AFR and received in exchange therefor 2,910 shares of preferred stock. In December 1959, deMontmollin surrendered additional AFR debentures and notes in the total face amount of \$31,000, which she owned, and received in exchange 310 shares of preferred stock. (PTO 40.)

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5. "EX." followed by a number or letters refers to exhibits in evidence.

"Tr." followed by a number refers to pages of the trial transcript.



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On April 1, 1960, the Burlington debentures held by Buchman and deMontmollin became due. Buchman was paid the interest and \$12,000 principal owing on his Burlington debentures on or about their due date. (PTO 38.) DeMontmollin's Burlington debentures in the amount of \$15,000 were also discharged and she received a credit for that amount on Burlington's books. She then loaned this same \$15,000 to AFR, then the parent company of Burlington, and received a note from AFR in that amount.

Buchman was paid the interest and principal amount owing on his Series A AFR debentures on or about their due date, May 1, 1960. (PTO 38.)

On January 17, 1961, AFR filed a voluntary petition for an arrangement under Chapter XI of the Bankruptcy Act and was duly adjudged a bankrupt on February 21, 1961. A Trustee in Bankruptcy was appointed on February 23, 1961. (PTO 2 and 3.) The Trustee has insufficient assets in his hands to pay in full the liabilities of said bankrupt. (PTO 5.)

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While Buchman was paid interest on his Series B AFR debentures until and including August 1, 1960, he has been paid neither any part of the \$64,000 principal nor any interest thereon falling due after August 1, 1960. AFR's Series B debentures were due on August 1, 1965. (EX. 37.)

Claiming breach of the subordination provisions of the Buy-Sell Agreement, Buchman instituted suit against the individual defendants in June 1960. (Buchman died on November 4, 1965 whereupon plaintiffs herein were duly appointed executors of his estate.) Jurisdiction is based upon diversity of citizenship. The complaint, as amended by the Pre-Trial Order, asserts that each of the three transactions enumerated above, to wit, the sale of Pathy's Series B AFR debentures to deMontmollin, the exchange of deMontmollin's AFR debentures for preferred stock, and the discharge of deMontmollin's Burlington debentures and loan by her of \$15,000 to AFR, constituted a breach of the subordination provisions. Relief is sought against the individual defendants, jointly and severally, in the amount of \$64,000 with interest from June 1, 1957.



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The issue confronting this Court, as framed in the Pre-Trial Order, is rather simply stated: "Did the individual defendants by their actions and conduct breach the subordination provisions of the May 17, 1957 agreement [Buy-Sell Agreement] entered into by them with Samuel Buchman?" (PTO VIII(a).) It is to a closer look at each of the transactions in question that we now turn.<sup>6</sup>

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6. During the course of the trial, decision was reserved on a number of evidentiary rulings. We now proceed to dispose of them: individual defendants' motion to strike Exhibit 34 is denied; individual defendants' objections to Exhibits 39, 41 and 42 for identification are overruled and those exhibits are admitted in evidence; plaintiffs' motion to strike Exhibit ES is denied; plaintiffs' objections to Exhibits EV, EW, EX and EY for identification are sustained; plaintiffs' objection to Exhibit EZ for identification is overruled and that exhibit is admitted in evidence. Decision was also reserved on individual defendants' motion to dismiss made at the end of plaintiffs case. That motion is hereby denied.

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The Sale Transaction

On June 1, 1957, Pathy sold his Series B AFR debentures to deMontmollin receiving \$80,000 from her in payment thereof. Plaintiffs contend that this transfer of debentures constituted a breach of the subordination provisions of the Buy-Sell Agreement.

In an attempt to establish such breach, plaintiffs have endeavored to draw a distinction between the second and third paragraphs of subparagraph A of the SIXTH paragraph of the Buy-Sell Agreement. Plaintiffs argue that while the third paragraph covers only payments received from the corporations on the debentures, the second paragraph is not so restricted in terms of "source of payment." Relying on this presumed distinction, they contend that the proceeds of the sale should have been used to reduce the amounts owing on Buchman's debentures.<sup>7</sup>

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7. Plaintiffs' Memorandum Submitted At The Conclusion Of The Trial, p.6.



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This argument is rebutted by the unambiguous language of the subordination provisions themselves. The clear purport of those provisions was to prohibit the individual defendants from receiving any payment of principal or interest from the corporations on their debentures until Buchman's debentures had been satisfied in full. Payment, upon sale and transfer of the debentures, from a source other than the corporations (here deMontmollin) was not prohibited by the provisions in question.

It is equally clear from the language employed that the possibility of future transfer of the debentures was recognized and permitted by the parties. The subordination provisions contemplated the possibility of holders of the debentures other than Pathy and deMontmollin and expressly provided for subordination of the debentures in the hands of "any holder."<sup>8</sup>

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8. The subordination provisions in part provided: "...Marie Louise deMontmollin and Alexander F. Pathy hereby agree with respect to the debentures of each of said corporations that the rights of any holder (including her or him) of the debentures thereof now held by her or him ...;" and

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Pathy's sale of his Series B AFR debentures to deMontmollin did not breach the subordination provisions of the Buy-Sell Agreement; his debentures (now owned by deMontmollin) remained subordinated to the debentures held by Buchman.<sup>9</sup>

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Footnote 8 cont'd

"[i]f for any reason, either corporation shall pay interest or principal on said debentures to any of the Buyers or to any person deriving title to the debentures of said corporation from any of the Buyers ...." (EK. 40.)

Individual defendants assert that "it is inconceivable that the parties would have written into the Agreement the phrase 'any holder (including her or him)' if the Agreement forbade there being any holder other than 'her or him.'" (Individual Defendants' Memorandum After Trial, p. 50.) We fully agree.

9. See Calligar, Subordination Agreements, 70 Yale L. J. 376, 399 (1961).



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We recognize that the transfer of Pathy's debentures may have violated the terms of the Subordination Agreement (Exhibit EH-1) entered into between The Pennsylvania Company For Banking and Trusts (hereinafter the Pennsylvania Bank), AFR, and Buchman, Pathy and deMontmollin.<sup>10</sup> Breach, if any, of that agreement, however, is not the issue presently confronting us; the

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10. Paragraph 9 of that Agreement provided: "Creditors [Buchman, Pathy, and deMontmollin] agree that so long as there remains any Indebtedness of Borrower to Bank, Creditors will not assign or transfer any of Borrower's Indebtedness to Creditors or any instrument evidencing the same, and in the event of any such assignment or transfer the Creditor so assigning or transferring shall thereupon immediately become liable to Bank in the amount of the Indebtedness so assigned or transferred."

There is absolutely nothing in the Buy-Sell Agreement which even intimates that the parties intended to have this prohibition on transfer become a part of their agreement. Further, the two agreements were not co-extensive in duration.

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the Pennsylvania Bank is not a party to the instant suit. Our concern rather is with an entirely separate agreement, the terms of which vary widely from those of Exhibit EN-1. Paragraph 9 of that exhibit, supra note 10, typifies language used where transfer of the subordinated debt is sought to be prohibited. The subordination provisions of the Buy-Sell Agreement, however, contain no similar prohibition on transfer; to the contrary, as previously discussed, they allow it.

#### The Exchange Transaction

In May 1958 and December 1959, deMontmollin surrendered debentures and promissory notes aggregating \$322,000<sup>11</sup> to AFR and received 3,220 shares of preferred

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11. Individual defendants' state that "[i]n and by the exchange, debts of the COMPANY aggregating \$300,000, owed to Mrs. deMontmollin, were turned into equity investments. \$231,000 of the \$300,000 was represented by debentures which were subordinated to BUCHMAN'S debentures. \$69,000 was represented by notes...." (Individual Defendants' Memorandum After Trial, p.23.) While these figures are inaccurate (the debts of the corporation converted into preferred stock aggregated \$322,000 (PRO 40); the subordinated debentures converted could not possibly have totaled \$231,000 since,



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stock in exchange therefor. Did this conversion of subordinated debt into equity violate the subordination provisions of the Buy-Sell Agreement? Resolution of this novel issue requires an understanding of the nature and effect of the subordination provisions and of the relationship created by them between Buchman (the senior creditor<sup>12</sup>) and the individual defendants (the junior creditors).<sup>13</sup>

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Footnote 11 cont'd

with the exclusion of deMontmollin's Burlington debentures which were not converted, the AFR debentures subordinated to Buchman's debentures only totaled \$222,000), we feel safe in assuming that deMontmollin converted all of her Series A and B AFR debentures (inclusive of those she acquired from Pathy) which were subordinated to Buchman's debentures.

12. "Senior creditor" refers to the holder of the senior debt. "Junior creditor" refers to the subordinator or the holder of the subordinated debt.
13. Pathy held no subordinated debentures at the time of the exchange. His Series B debentures which were sold to deMontmollin in June 1957 were exchanged by her for preferred stock.

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The subordination provisions had two principal effects. First, as already discussed, the individual defendants were expressly prohibited from receiving any payment of interest or principal from the corporations on their debentures until all of Buchman's debentures had been fully satisfied. This prohibition ensured that the corporations' assets would not be reduced by payments on the subordinated debts until Buchman's debentures had been fully paid. If any payments of interest or principal were received by the individual defendants before Buchman's debentures were fully satisfied, such amounts, by the terms of the subordination, were to be promptly paid to Buchman. This type of agreement, under the terms of which "no payment of principal or interest on the subordinated debt is permitted . . . so long as specifically identified senior debt remains unpaid," is commonly referred to as a "complete" subordination.<sup>14</sup>

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14. Calligar, supra note 9, at 378. See also Coogan, Kripke, and Weiss, The Outer Fringes of Article 9: Subordination Agreements, Security Interests In Money And Deposits, Negative Pledge Clauses, And Participation Agreements, 70 Harv. L. Rev. 229, 234 (1965); 2 Gilmore, Security Interests in Personal Property §37.1 at 986 (1965).



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Second, while subordination "suggests a mere ranking of priority, upon the insolvency of the common debtor the amounts otherwise payable on the junior creditors claim will in the usual subordination situation be payable to the senior creditor."<sup>15</sup> Thus, subordination has "the practical effect of making the subordinated debt a type of security for the senior debt, available to the senior creditor upon a distribution of the assets of the debtor."<sup>16</sup> Stated another way, the subordinated debt has a "collateral value" to the senior creditor in the event of the common debtor's insolvency which justifies his regarding it as a "cushion" or "support" for his senior debt.<sup>17</sup> Whether a junior creditor

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15. Coogan, Kripke, and Weiss, supra note 14, at 236 n.25.

16. Calligar, supra note 9, at 378.

17. Golin, Debt Subordination As A Working Tool, 7 N.Y.L. P. 370, 379 (1961); Everett, Subordinated Debt-Nature, Objectives and Enforcement, 44 Boston Univ. L. Rev. 487, 524 (1964); Coogan, Kripke and Weiss, supra note 14, at 236 n.25. One commentator has stated that "[t]he [senior] creditor is advantaged by obtaining, either specifically for itself or generally with other creditors, a collateralized position and a resulting superior right of distribution to the debtor's assets." Golin, supra at 379. See also 2 Gilmore, supra note 14, § 37.1 at 985-86.

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(here deMontmollin) could extinguish this so-called "security" or "cushion" without breaching the subordination provisions is an issue we reserve for later discussion.

Much of the trial record<sup>18</sup> concerns itself with the conflicting positions taken by the parties on the meaning of the word "payment" found in the subordination provisions. Plaintiffs, contending that "payment" means "the transfer of consideration which discharges a debt,"<sup>19</sup> argue that deMontmollin's receipt of preferred stock in exchange for her debentures constituted "payment" of those

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18. Pathy was the only witness to testify at trial.

19. Plaintiffs' Memorandum Submitted At The Conclusion Of The Trial, p. 12.

Plaintiffs place much reliance on the fact that Pathy understood the word "payment" -- as used in the last resolution of Exhibit 33 -- to mean "legal discharge." (Tr. 171.) The meaning attributed to "payment" when used in a different context and outside of the subordination provisions, is not controlling. We note, however, that the indebtedness of the corporation was "legally discharged" in and by the exchange. As will be explained, this does not mean that "payment," as that was used in the subordination provisions, was received on the debentures.



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debentures. The individual defendants, on the other hand, assert that "payment," as used in the subordination provisions, contemplated only payment with assets of the corporation; since no assets of the corporation were expended in discharging the debentures, they argue no "payment" was received. We agree with the position of the individual defendants.

While the exchange resulted in the discharge of the debentures as legal obligations of the corporation, the receipt of preferred stock in place thereof did not constitute "payment" (of interest or principal) as that term was used in the subordination provisions.<sup>20</sup> The clear intent of those provisions was to prohibit any payment out of the assets of the corporations on the individual defendants' debentures before Buchman's debentures were paid in full. No assets of AFR were paid out in discharging deMontmollin's debentures. The exchange

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20. Cf. McConnell v. Estate of Butler, 402 F.2d 362, 366 (9th Cir. 1968).

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did not affect the asset side of the corporation's balance sheet; only the liabilities and capital side was affected, i.e. long-term debt was converted into capital.<sup>21</sup>

In this Court's memorandum of May 9, 1967, denying individual defendants' first summary judgment motion,<sup>22</sup> we noted that the possibility that the exchange was "a first step in a plan to obtain cash -- or cash realizable property -- from the corporations" had not been excluded. In an effort to disprove the existence of such a plan, individual defendants sought to establish at trial that the prime objective of the exchange was to obtain a higher credit rating from Dunn & Bradstreet and other rating companies, and thereby increase the credit capacity and borrowing power of AFR. (Tr. 272-73.)

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21. See EXs. BP and EQ.

22. We denied individual defendants' second summary judgment motion on August 13, 1968.



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We need not determine whether the existence of such a plan (although never fully consummated) would constitute a breach of the subordination provisions since we are convinced that the exchange was not a first step in a plan by which the individual defendants, or any one of them, would obtain cash or its equivalent from the corporation. In fact, an examination of deMontmollin's status as a holder of preferred stock indicates that it was highly improbable that she would realize any cash or its equivalent out of the assets of AFR by means of the exchange.

The stock acquired through the exchange was five per cent (5%) cumulative preferred stock which was redeemable at any time by the corporation. (EX. EO.) As detailed below, AFR, however, was effectively precluded (at all times with which we are here concerned) from either paying dividends on, or redeeming any shares of, the preferred stock.

Each AFR Series B debenture provided for the payment of interest at the rate of five per cent (5%)

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per annum and for the payment on each interest payment date (commencing February 1, 1956) of five per cent (5%) of the respective principal amount thereof.<sup>23</sup> AFR agreed that "as long as any past due instalments of principal remain unpaid it will not declare any dividends upon any class of its capital stock ...." (EX. 37, ¶5.)

The corporation never paid any portion of the principal amount owing on Buchman's Series B debentures. (PTO 38.) In fact, until some time in 1959 when Walter E. Heller & Co. replaced the Pennsylvania Bank as the main source of financing for the corporation, AFR was prohibited by the terms of the Subordination Agreement with the Pennsylvania Bank<sup>24</sup> from making any payments on

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23. AFR was not "required to make any payment on account of principal if the undersigned has not accumulated earnings and profits at least sufficient in amount to provide for that payment." (EX.37, ¶5).

24. The parties to the instant litigation were also parties to that subordination agreement under the terms of which they agreed to subordinate their Series B debentures to AFR's indebtedness to the Pennsylvania Bank. (EX. EN-1.) See also subparagraph C of the SIXTH paragraph of the Buy-Sell Agreement. (EX. 40.)



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account of principal on its Series B debentures.<sup>25</sup>

(EX. EN-1, ¶8.) Accordingly, no dividends could be declared on the preferred stock since no instalments of principal were paid on Buchman's Series B debentures.

Redemption of the preferred shares was prohibited by the very terms of the Buy-Sell Agreement:

To induce the sale of capital stock hereunder, the Buyers warrant and agree that, until the entire purchase price hereunder shall have been paid in full and until all the debentures and the Promissory Note now held by Samuel Buchman (which are described in paragraph SIXTH hereof) shall have been paid in full, neither American Foam nor Burlington will redeem or purchase any of its capital stock or make any distribution to its stockholders in the nature of a liquidation or partial liquidation.... (EX. 40, EIGHTH paragraph.)

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25. AFR was permitted to make payments of interest (not in excess of 5% per annum) on the debenture bonds. (EX. EN-1, ¶12.)

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Additionally, while the Term Loan Agreement with the Pennsylvania Bank (Exhibit EN) remained in effect,<sup>26</sup> AFR had to refrain from purchasing or redeeming any of its capital stock or that of any of its subsidiaries "if the aggregate consideration for all of such purchases and redemptions exceeds \$10,000 in money or property." (Ex. EN, §4.11.)

It is clear from the foregoing that AFR could not redeem or purchase any of the shares of preferred stock issued to deMontmollin in exchange for her debentures. Further, no dividend payments could be made on said shares unless and until all past due instalments of principal on the outstanding Series B debentures were paid. Under such circumstances, we cannot comprehend the exchange as a first step in a plan to obtain cash or its equivalent from AFR.

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26. Burlington was also a signatory to that agreement.



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dividends paid on subordinated debt

While the exchange transaction did not result in deMontmollin receiving "payment" (as that term was used in the subordination provisions) of interest or principal on her debentures, it did have the adverse affect of depriving Buchman, and now his executors (the plaintiffs herein), of a "double dividend"<sup>27</sup> out of AFR's bankrupt estate -- i.e. the dividends paid on the senior debt and, by reason of the subordination provisions, the dividends paid on the subordinated debt. The following example illustrates why, from the point of view of the senior creditor, subordinated debt is preferable to equity:

[A]ssume that a bankrupt company has \$600,000 of assets and has outstanding \$500,000 of senior debt, \$500,000 of subordinated debt, and \$500,000 of other debt. On a distribution of all the assets

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27. Calligar, supra note 9, at 377; 2 Gilmore, supra note 14, § 37.1 at 985.

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of the company the senior debt would receive \$400,000 -- the \$200,000 dividend paid on the senior debt plus the \$200,000 dividend paid on the subordinated debt -- and the other debt would receive \$200,000. If the subordinated debt had been preferred stock, however, the senior debt would have received only \$300,000, with the remaining \$300,000 being paid on the other debt.<sup>28</sup>

Individual defendants are mistaken in arguing "[i]f nothing is paid out of assets it is of no consequence to the favored creditor that the subordinated debt is wiped out."<sup>29</sup> Buchman's "security" or "cushion" for his senior debt was lost when the subordinated debt was "wiped out." The exchange affected Buchman in the same way that a discharge of the subordinated debt by waiver, forgiveness, or cancellation would have, namely, he was deprived of the dividend -- the junior creditor's (here deMontmollin's) dividend -- on the subordinated debt.

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28. Calligar, supra note 9, at 377.

29. Individual Defendants' Memorandum After Trial, p. 41.



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Subordination agreements have long been upheld by the courts. In bankruptcy proceedings, the terms of subordination have been enforced with the result that the dividends paid on the subordinated debt are allocated to the senior debt.<sup>30</sup> This has been so despite the absence of any reference in the subordination agreements to bankruptcy proceedings.<sup>31</sup> Accordingly, had deMontmollin remained a creditor of APR, the dividends paid out of the bankrupt estate on her subordinated claims would have been allocated to Buchman's senior debt.

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30. Subordination Agreements have been enforced on a variety of theories. See 2 Coogan, Hogan, Vagts, Secured Transactions under U.C.C. § 23.02[3] at 2352 n.21; Calligar, supra note 9, at 383-92.

31. See In re Credit Industrial Corp., 366 F.2d 402, 412 (2d Cir. 1966). Cf. In re Aktiebolaget Kreuger & Toll, 96 F.2d 768, 770 (2d Cir. 1938).

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DeMontmollin, however, did not retain her junior creditor status; rather, through the exchange she became a stockholder of AFR thereby subordinating her claim against the corporation to the claims of all creditors. The "security" of a "double dividend" in the event of bankruptcy was lost to Buchman.

Did deMontmollin breach the subordination provisions when she altered her status from one of junior creditor to that of preferred stockholder? Was she prohibited by the terms of the subordination from discharging the subordinated debt?

Individual defendants<sup>32</sup>, citing no authority, vigorously contend that it is "preposterous" to believe that subordination forbids discharging ("wiping out") the subordinated debt.<sup>32</sup> We must disagree. The authority that exists, scant though it may be, points convincingly in the opposite direction.

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32. Individual Defendants' Reply Memorandum, p. 13.



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In In re Dodge-Freedman Poultry Co.,<sup>33</sup> Freedman,

the president, director, and principal stockholder of Dodge-Freedman Poultry Company, in consideration for credit extended by Delaware Mills to the Poultry Company, agreed to subordinate all of his claims against the Poultry Company (totaling \$50,000) to the debt owed by the Poultry Company to Delaware Mills, and further agreed that no payments would be made to him until all amounts owing to Delaware Mills had been paid. In 1955 the Poultry Company filed a petition for an arrangement under Chapter XI of the Bankruptcy Act. A Plan of Arrangement was subsequently adopted providing for payment of a fifteen per cent (15%) dividend to all unsecured creditors in full satisfaction of their claims. One such unsecured claim was the \$50,000 owing to Freedman;

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33. 148 F.Supp. 647 (D.N.H. 1956), aff'd sub nom., Dodge-Freedman Poultry Co. v. Delaware Mills, Inc., 244 F.2d 314 (1st Cir. 1957).

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by the terms of the Arrangement, he was entitled to receive a dividend of \$7,500 on his claim. Before payment, however, Freedman waived all rights to share in any dividend under the plan.<sup>34</sup>

Delaware Mills, having received a 15% dividend on its own claim, filed another proof of claim asserting its right to an additional dividend of \$7,500 (the dividend Freedman would have received had he not waived his claim) by virtue of the subordination agreement.

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34. The \$50,000 claim was both proved and waived by Mrs. Freedman. For purposes of the proceeding, however, it was agreed to consider the claim filed and waived by her as being a claim of Freedman.



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The court, in upholding Delaware Mills' right to Freedman's dividend, made the following pertinent observations:

The forbearance agreement prevented him [Freedman] from collecting and retaining any money on his own behalf so long as Delaware's claim had not been satisfied up to the agreed sum. As a result, it might seem that Freedman was actually fulfilling his contract when he waived all rights, because he was, in effect, forbearing. But equity will regard the substance rather than the form of every agreement and examine its purpose and intent. [citation omitted.] Applying this principle to the contract, it is obvious from its language that its intent and purpose was that Delaware's claim would be 'satisfied and paid.' Therefore, by looking behind the mere formality of forbearance, equity can take cognizance of the fact that Freedman, to a limited extent, undertook to assure payment of Delaware's claim up to \$50,000. Although it is true that Freedman had no duties to perform other than to forbear, he is, at the very least, barred by the spirit of the agreement from taking any action that might prevent the satisfaction of Delaware's claim. By waiving his right to a dividend, Freedman is doing just that. He is returning the money to the debtor against whom Delaware Mills has no further rights since it has already accepted its full, legal share under the Plan of Arrangement. Thus Freedman was estopped from waiving his claim, for to do so violates the intent and purpose behind the agreement.<sup>35</sup>

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35. In re Dodge-Freedman Poultry Co., supra note 33, at 651.

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The court went on to enforce the subordination agreement by holding Freedman to be a "constructive trustee" for Delaware Mills.

The facts of our own case are in some respects quite similar to those in Dodge-Freedman. Here we have a situation where a junior creditor, who was a principal stockholder, director and officer of the common debtor, through the expedient of the exchange transaction, discharged the subordinated debt. There apparently was no way for Buchman, at the time he entered into the Buy-Sell Agreement, to anticipate this happening. This is not a case where a senior creditor should have been cognizant of the consequences of debenture provisions allowing conversion of the subordinated debt into capital stock. AFR's Series A and B debentures contained no provisions permitting conversion (at the option of the holder) into capital stock.<sup>36</sup> Conversion became possible only after the

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36. We have not been informed of the provisions of AFR's Series A debentures. We assume, from the silence of the parties, that they, like the Series



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individual defendants in their capacities as officers, directors and stockholders of AFR caused the certificate of incorporation to be amended to provide for preferred stock, and thereafter passed the resolution allowing preferred shares to be issued in exchange for Series A and B debentures surrendered to the corporation. (EX. FD.)

We note that our problem presents an aspect which differs from that confronting the court in Dodge-Freedman. Here the subordinated debt was discharged considerably before the filing of AFR's voluntary petition for an arrangement under the Bankruptcy Act.<sup>37</sup> This distinction notwithstanding,

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Footnote 36 cont'd

B debentures contained no provision permitting conversion into capital stock.

37. The exchange of debentures for stock took place in May 1958 and December 1959. AFR filed a voluntary petition under Chapter XI of the Bankruptcy Act on January 17, 1961. The Corporation was adjudged a bankrupt in February, 1961.

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we believe that the reasoning which estopped Freedman from waiving his dividend is fully applicable here.<sup>38</sup>

It matters not that the subordinated debt was discharged before bankruptcy rather than after; the effect on the senior creditor, i.e. loss of the dividend on the subordinated debt, is identical in both cases.<sup>39</sup>

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38. While relying on that portion of the court's reasoning previously set out in the body of this opinion, we recognize the inapplicability of the constructive trust theory to the facts of this case. See Cherno v. Dutch American Mercantile Corp., 353 F.2d 147, 154 (2d Cir. 1965).

39. "In light of the attempt made by the subordinator in Dodge-Freedman to escape the consequences of his subordination," one commentator has suggested that "it might be well to insert in future subordination agreements a provision prohibiting waiver, forgiveness, or cancellation of the subordinated debt." Calligar, supra note 9, at 387-88.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

In Cherno v. Dutch American Mercantile Corp.,<sup>40</sup>

Blanmill Realty Corp., in consideration for Dutch American loaning Itemlab, Inc., \$50,000 on Itemlab's note in that amount, agreed that its claim against Itemlab for \$87,000, evidenced by a note and secured by a chattel mortgage, "shall \* \* \* be subject and subordinate in lien to the lien of said note for \$50,000," and that "no part of the indebtedness \* \* \* shall be paid [to Blanmill] until all sums due and owing to Dutch American Mercantile Corp. shall have been paid and disposed of."<sup>41</sup>

Itemlab defaulted on its note to Dutch American, and the latter commenced an action to recover the amount due. While that case was pending, Blanmill "executed and filed a satisfaction of the chattel mortgage in spite of the fact that no part of the mortgage

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40. 353 F.2d 147 (2d Cir. 1965).

41. 353 F.2d at 149.

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debt had ever been paid."<sup>42</sup> An innocent third party, relying on such discharge, thereafter loaned funds to Itemlab on the security of the same chattels. Upon Itemlab's bankruptcy the chattels were sold and Dutch American claimed the proceeds of the sale. The court denied Dutch American's claim to the proceeds holding that the subordination agreement did not result in an equitable assignment of the subordinated debt on the chattel mortgage.<sup>43</sup> The court also rejected the assertion that an equitable lien on, or constructive trust of,<sup>44</sup>

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42. Id.

43. The court further held that even if an assignment did result, the law of New York required that it be recorded to be effective against third parties.

44. While the court rejected Dutch American's claim to the proceeds of the chattels, it did hold that "if, at the conclusion of the bankruptcy proceedings in Itemlab, Inc., debtor, liquidation had been accomplished and a distributive dividend were ordered to Blanmill and Dutch American, as creditors, Dutch American, on the theory of constructive trust, could, to the extent of its claim, receive Blanmill's dividend under the subordination agreement and prevent Blanmill from taking it and using it for its own purposes." 353 F.2d at 154.



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the chattels or their proceeds resulted from the subordination.

The importance of this case for present purposes arises from the following statement by the court:

Dutch American at no time had an interest in or lien upon the chattels. Its so-called "security" was nothing more than a promise by Blannmill to apply no payment against the mortgage debt until Dutch American was paid in full. Blannmill breached that agreement, but breach of a contract concerning payment of a debt furnishes no basis for the finding of a constructive trust. [citation omitted.] Dutch American could enforce the obligation against Blannmill and Itemlab as parties to the subordination agreement but not against other existing or subsequent creditors. (Emphasis supplied.)<sup>45</sup>

The court's statement that Blannmill breached the subordination agreement could only have reference to its discharge of the chattel mortgage.<sup>46</sup> We interpret

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45. 353 P.2d at 154.

46. No part of the debt which the mortgage was intended to secure was paid.

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the court as saying that the junior creditor's discharge of the chattel mortgage securing the subordinated debt constituted a breach of the subordination agreement.<sup>47</sup> If this is so, and we have no reason to

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47. It is significant to note that in the converse situation, i.e. release by a senior creditor of collateral security held for the senior debt, the junior creditor would be adversely affected.

"To the extent that such collateral is not available to the senior creditor in the event of the bankruptcy of the debtor, dividends on the subordinated debt must be used in making the senior creditor whole. In other words, by giving up his collateral, the senior creditor makes it more likely that if the debtor goes bankrupt, the senior creditor will have to satisfy the obligation owed him by taking the junior creditor's dividends. It would therefore follow, in the absence of a provision permitting the senior creditor to alter the terms of the debt or deal with the security therefor that the senior creditor might be obliged to some extent to the subordinating creditor as to the value of the collateral released." Calligar, supra note 9, at 530-31.

Professor Gilmore has stated: "No doubt release or impairment of collateral by a secured senior should pro tanto release the unsecured subordinator from his duties under the subordination agreement just as it would release a surety." 2 Gilmore, supra note 14, § 37.1 at 985-86 n.10.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
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doubt that it is, then discharge of the subordinated debt itself most certainly constitutes a breach of the subordination.

The foregoing authorities convince us that deMontmollin's discharge of her Series A and B AFR debentures by means of their exchange for preferred stock constituted a breach of the subordination provisions of the Buy-Sell Agreement. Buchman's contemplated right to the dividend which would have been paid on the subordinated debt, had it not been discharged, was lost by virtue of the exchange. The absence of any express reference in the subordination provisions to either distributive dividends on bankruptcy is not controlling.<sup>48</sup> Implicit in the language used is the intent of the parties that Buchman have the "security"<sup>49</sup>

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48. See cases cited in note 31, supra.

49. The "security" that comes from the senior creditor's right to the distributive dividend paid on the subordinated debt.

OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

of the subordinated debt in the event of the common debtor's bankruptcy. This "security" was lost to Buchman just as it was lost to Dutch American in Cherno<sup>50</sup> and almost lost to Delaware Mills in Dodge-Freedman. At the very least, deMontmollin was barred by the terms of the subordination from taking any action that might prevent satisfaction of Buchman's claim.<sup>51</sup> Her exchange of debentures for preferred stock had just that effect.

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50. Dutch American did not lose all its "security" since Blanmill still held Itemlab's note for \$87,000. See note 44, supra.

51. A subordinator has been referred to as "a guarantor to the extent of the value of the subordinated debt." Calligar, supra note 9, at 394. But see Golin, supra note 17, at 371, where issue is taken with this characterization.



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Leading commentators have devoted considerable energy to the question: "Does a subordination create an article 9 security interest against the junior creditor and in favor of the senior creditor?"<sup>52</sup> The answer to this question becomes important in situations where both the common debtor and the junior creditor have gone bankrupt<sup>53</sup> since there the issue of priority between the senior creditor and the junior creditor's trustee in bankruptcy is a very real one.<sup>54</sup>

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52. Coogan, Kriphe and Weiss, supra note 14, at 236. See also 2 Coogan, Hogan, Vagts, supra note 30, ch. 23; 2 Gilmore, supra note 14, § 37.3 at 994.

53. See Pioneer-Cafeteria Foods, Ltd. v. Mack, 340 F. 2d 719 (6th Cir. 1965).

54. If the senior creditor has acquired a security interest, and it does not meet the enforcement and perfection requirements of Article 9 of the Uniform Commercial Code, "it is not good against the junior creditor's trustee in bankruptcy. Coogan, Kripke, and Weiss, supra note 14, at 235.

OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
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We are not here faced with such a dilemma (plaintiffs seek only to recover against a junior creditor for her breach of the subordination provisions of the Buy-Sell Agreement), and accordingly intimate no view on the "true nature" of the interest created, if any, in favor of a senior creditor by virtue of a subordination agreement. We hold only that where a subordination agreement is in effect, in the absence of provisions to the contrary, it is a breach of that agreement for a junior creditor to discharge the subordinated debt as was done here.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

The Loan Transaction

On April 1, 1960, deMontmollin's Burlington debentures aggregating \$15,000 became due and payable. At some point (apparently in April) she surrendered these debentures to Burlington and received a credit for \$15,000 on Burlington's Books. (Tr. 24.)<sup>55</sup> De Montmollin then proceeded to loan this same \$15,000 to AFR and received a note<sup>56</sup> from AFR in that amount.<sup>57</sup>

55. DeMontmollin could draw against those funds from the time of credit to her account. (Tr. 26.)

56. Exhibit 36 states: "The loans [including de Montmollin's] are represented by 6% notes maturing on December 30, 1960. Interest thereon has been paid through December 31, 1960."

57. Pathy described the transaction in question as follows:

"[I]n April of 1960, Mrs. deMontmollin, who was supposed to receive \$15,000 on her A bond Burlington debentures did not receive \$15,000 on those bonds, but loaned those \$15,000 to AFR." (Tr. 161.)

"She had Burlington Holding bonds or debentures which matured in April of 1960. By that time Burlington was a subsidiary of American Foam. The same amount of \$150,000 [sic] which were [sic] supposed to be paid to her but were [sic] not paid, were [sic] loaned by her to AFR and therefore it became a loan of an officer to AFR." (Tr. 173)

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This series of "bookkeeping entries" had four principal effects: first, deMontmollin's Burlington debentures were discharged;<sup>58</sup> second, the assets of Burlington were reduced by \$15,000 -- the amount loaned by deMontmollin to AFR;<sup>59</sup> third, the assets of AFR were increased by \$15,000; and fourth, deMontmollin

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58. The debentures ceased to be obligations of the corporation and the principal amount owing on them was credited to deMontmollin's account on Burlington's books. Burlington still owed de Montmollin \$15,000 (evidenced by the credit to her account) but not by virtue of the debentures.

59. It is undisputed that the \$15,000 loaned to AFR was the same \$15,000 payable on the Burlington debentures. The \$15,000 credit to deMontmollin's account must have been extinguished by her loan of those funds to AFR. This debit to her account must have been accompanied by a corresponding credit to Burlington's cash account.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

became a note holder of AFR for the amount of the loan.<sup>60</sup>  
Viewed with these effects in mind, it becomes apparent  
that the loan transaction resulted in deMontmollin re-  
ceiving "payment" on her Burlington debentures.

While deMontmollin did not "physically" re-  
ceive cash (or its equivalent) from Burlington, she  
did receive a credit on Burlington's books for \$15,000  
which amount she then chose to loan to AFR. Certainly  
the fact that the funds did not "physically" pass  
through her hands on their way to AFR is not controlling.  
The effects of the transaction would have been exactly  
the same had she had Burlington pay her the \$15,000 be-  
fore she loaned it to AFR.

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60. Counsel for individual defendants, during the  
course of the trial, stated that "the \$15,000  
note which was taken by Mrs. deMontmollin in  
April 1960 and which was never paid, was as-  
signed to an attorney, and that is a claim in  
the bankruptcy proceeding." (Tr. 50.)

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Clearly deMontmollin cannot get around the subordination provisions' prohibition on "payment" of her debentures by the series of "bookkeeping entries" involved here.<sup>61</sup> Her realization of "payment" in the amount of \$15,000 on her Burlington debentures is attested to by the fact that she loaned these very funds to AFR.<sup>62</sup>

We hold that the loan transaction resulted in de Montmollin receiving "payment" of \$15,000 on her Burlington debentures. By the terms of the subordination, she was required to promptly pay that amount over to Buchman. In failing to do so, she breached the subordination provisions of the Buy-Sell Agreement.

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61. We cannot accept Pathy's oversimplified characterization of the transaction as simply a "bookkeeping device by virtue of which the indebtedness of the subsidiary [Burlington] became the indebtedness of the parent Co. [AFR]" without any amount being paid to deMontmollin. (Tr. 173, and 257.)

62. We intimate no view on whether the credit to her account standing alone, i.e. unaccompanied by the loan to AFR, constituted the receipt of "payment" resulting in the amount credited having to be paid to Buchman.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

Damages

Before turning to the matter of damages, one preliminary point warrants attention. Plaintiffs seek to recover against the individual defendants "jointly and severally." No reason is assigned, however, why breach of the agreement by any one of the individual defendants should result in liability being imposed "jointly" on all of them. There is nothing in the Buy-Sell Agreement indicating that the individual defendants agreed to be "jointly" responsible for any breach of the subordination provisions.<sup>63</sup> It appears not to have been their intent to enter into a joint agreement with respect to subordination. Rather, each agreed to subordinate his or her own debentures to those debentures held by Buchman. The agreement was several not joint.

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63. Contrast subparagraph F of the THIRD paragraph of the Buy-Sell Agreement where Pathy expressly agreed to guarantee the obligations thereunder of Suzanne M. Pathy.

OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

There is nothing before us to warrant the imposition of liability on Suzanne M. Pathy and Alexander F. Pathy. The former was not herself a subordinator, and the latter, while a holder of subordinated debt,<sup>64</sup> never breached the subordination provisions.<sup>65</sup> Only de Montmollin breached those provisions -- only to the extent hereinabove discussed -- and, accordingly, only she is liable to plaintiffs for the damages sustained by Buchman.

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64. We have already held that Pathy's transfer of his Series B AFR debentures to deMontmollin was not in breach of the subordination provisions.

65. The fact that both the Pathys were officers and directors of AFR, and, as such, had a hand in passing the resolution allowing the exchange of debentures for stock is far from decisive. It was only deMontmollin who exchanged her debentures for stock and thereby extinguished the subordinated debt.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

Both the exchange and loan transactions have been found to breach the subordination provisions of the Buy-Sell Agreement; the amount of damages resulting therefrom is the only issue remaining for determination.

Plaintiffs, without any specificity or breakdown of any sort, assert that they are entitled to \$64,000 with interest from June 1, 1957. Individual defendants, on the other hand, contend that even if the subordination provisions were breached, "Buchman suffered no damage therefrom."<sup>66</sup> Both are wrong.

Buchman was certainly damaged when deMontmollin, in breach of the subordination provisions, failed to turn over the \$15,000 she realized on her Burlington debentures. Accordingly, plaintiffs are entitled to recover that amount plus interest thereon from the date of such breach.

The damage resulting from deMontmollin's exchange of her AFR debentures for preferred stock is not

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66. Individual Defendants' Memorandum After Trial, p.65.

OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

as readily ascertainable. We have already seen that the exchange adversely affected Buchman by depriving him of the distributive dividends that would otherwise have been paid on the subordinated debts. Had deMontmollin remained a junior creditor of AFR, the dividends paid out of the bankrupt estate on her subordinated claims would have been allocated to Buchman's senior debt. Plaintiffs, therefore, are entitled to the amount of such dividends lost to Buchman as a result of the exchange; that is, the amount of the dividends deMontmollin would have been entitled to out of AFR's bankrupt estate had she not converted her debentures into stock.

Plaintiffs, unfortunately, have failed to furnish this Court with sufficient information upon which to predicate a computation of deMontmollin's distributive dividends.<sup>67</sup> Therefore, we are faced with this additional

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67. Exhibit 39 does reveal that the assets in the hands of the Trustee amount to \$91,179.35 while the total general claims aggregate \$2,011,318.21.



OPINION OF IRVING BEN COOPER, U.S.D.J. DATED  
JULY 23, 1969

challenge: Should we dismiss the claim because of a failure of proof in respect of damages (the trial record now being closed) or should we attempt to secure further information upon which damages may be predicated. We have decided to adopt the latter course.

X Accordingly, the question still to be resolved is as follows: Assuming deMontmollin presently held the Series A and Series B AFR debentures she converted into preferred stock, what would be the total amount of dividends thereon that she would receive out of the bankrupt estate? In order to satisfactorily respond to this question, which we regard as expressing the formula upon which damages are to be predicated the parties are allowed fifteen (15) days from the date of this Opinion to serve and file proof in affidavit form addressed to this sole remaining issue. We hereby request the Trustee in Bankruptcy (to whom a copy of this Opinion on its filing date will be mailed) to aid the parties in their efforts to resolve this question. X

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JULY 23, 1969

As to liability only, the foregoing shall  
constitute this Court's Findings of Fact and Con-  
clusions of Law.

New York, N.Y.  
July 23, 1969

IRVING BEN COOPER

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UNITED STATES DISTRICT JUDGE



OPINION OF HON. IRVING BEN COOPER, U.S.D.J. DATED  
SEPTEMBER 26, 1969.

**UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK**

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**FIRST NATIONAL BANK OF HOLLYWOOD,  
et al.,**

**Plaintiffs,**

**-against-**

**AMERICAN FOAM RUBBER CORPORATION,  
et al.,**

**Defendants.**

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60 Civ. 2328

MEMORANDUM

**IRVING BEN COOPER, D. J.**

Plaintiffs' second cause of action charging the individual defendants with having breached the subordination provisions of the Buy-Sell Agreement entered into between them and Samuel Buchman on May 17, 1957 was tried to this Court. In an opinion filed July 23, 1969, we held that Marie Louise deMontmollin had breached the provisions in question when she exchanged her American Foam Rubber Corporation (AFR) debentures for preferred stock and when she discharged her Burlington debentures and loaned \$15,000 to AFR. We found that the latter

OPINION OF HON. IRVING BEN COOPER, U.S.D.J. DATED  
SEPTEMBER 26, 1969

breach damaged plaintiffs to the extent of \$15,000,  
plus interest thereon from the date of such breach.

The damages resulting from the exchange of debentures for preferred stock were not as readily ascertainable. We expressed the formula by which such damages were to be computed as follows: "Assuming deMontmollin presently held the Series A and Series B AFR debentures she converted into preferred stock, what would be the total amount of dividends thereon that she would receive out of the bankrupt estate?" (Opinion of this Court, dated July 23, 1969, p.51.) Determination of the damages resulting from the exchange was rendered impossible, however, by plaintiffs' failure to furnish the court with sufficient information upon which to predicate a computation of deMontmollin's distributive dividends. So confronted, we chose to allow the filing of additional proof in affidavit form.

Both sides have submitted affidavits and reply affidavits addressed to this specific issue of damages. Plaintiffs seek to recover \$10,656; defendants contend



OPINION OF HON. IRVING BEN COOPER, U.S.D.J. DATED  
SEPTEMBER 26, 1969

they are entitled to only \$2,112. While the dollar distance between the parties on this specific damage item involves a relatively small amount, their papers clearly point up how speculative and uncertain would be the factors upon which such damages could be predicated if computed at this time. Even the taking of extensive testimony (as defendant asserts is necessary) would present the same handicaps if undertaken now.

This case is unique in that while such damages are highly conjectural today they can be made certain at some future date. Plaintiffs' damages in this respect are measured by the distributive dividend paid out by the bankrupt estate to its general unsecured creditors; this dividend, of course, must be adjusted for our purposes by adding deMontmollin's claim (apparently \$222,000) to the claims of other general unsecured creditors. The amount of this distributive dividend will become ascertainable at some future date. We firmly believe that it would be unwise as well as unfair to all parties concerned to presently do otherwise.

OPINION OF HON. IRVING BEN COOPER, U.S.D.J. DATED  
SEPTEMBER 26, 1969

Accordingly, confronted by no reasonable alternative, we have resolved to hold the computation of the aforementioned specific damages in abeyance until the amount of the dividend to be paid out by the bankrupt estate can be ascertained with a reasonable degree of certainty. We note that this places plaintiffs in almost the same position they would have been in had deMontmollin not converted her debentures into stock, i.e., in the absence of such a breach, plaintiffs would have had to await distribution of the bankrupt estate before receiving the dividend paid on deMontmollin's claim.

Since entry of judgment on plaintiffs' second cause of action must await determination of the aforementioned damages, and since "there is no just reason for delay," we direct that judgment be entered on all other claims in this litigation. Rule 54(b), F.R.Civ.P. Entry of judgment shall not be delayed for the taxing of costs. Rule 58, F.R.Civ.P.

The parties shall submit forms of judgment on notice within 10 days from this date.

New York, N.Y.  
September 26, 1969

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UNITED STATES DISTRICT JUDGE



EXCERPT FROM MEMORANDUM OPINION OF HON. IRVING  
BEN COOPER, DATED SEPTEMBER 26, 1969.

**UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK**

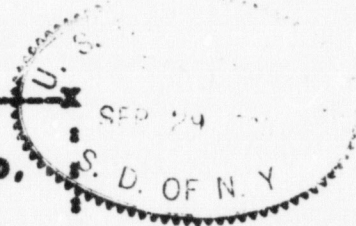
**FIRST NATIONAL BANK OF HOLLYWOOD,  
et al.,**

**Plaintiffs,**

**-against-**

**AMERICAN FOAM RUBBER CORPORATION,  
et al.,**

**Defendants.**



**60 Civ. 2328**

**MEMORANDUM**

**IRVING BEN COOPER, D. J.**

The Trustee in Bankruptcy of American Foam Rubber Corporation (AFR) moves to have pre-verdict interest added to the \$20,000 jury verdict returned on April 29, 1968 in his favor on his first counterclaim charging Samuel Buchman with conspiring with other employees of AFR to injure or destroy that corporation's business.

JUDGMENT ENTERED OCTOBER 14, 1969.

UNITED STATES DISTRICT COURT,  
SOUTHERN DISTRICT OF NEW YORK.

The above entitled action having been assigned for all purposes to HON. IRVING BEN COOPER, United States District Judge:

And defendant ACKMAN'S Second Counterclaim and Cross-Claim in the above entitled action having been on October 25, 1965, dismissed on cross motions for summary judgment made by plaintiffs' deceased predecessor, SAMUEL BUCHMAN, and defendants de MONTMOLLIN and PATHY; and, the Pre-Trial order herein having be consent directed judgment for plaintiffs on their First Cause of Action as herein below decreed;

And the remaining issues in said action having come on regularly for trial before the said District Judge, and a jury on April 1st to and including April 29, 1968 as to defendant ACKMAN'S First Counterclaim and the counterclaim of said defendants de MONTMOLLIN and PATHY and non-jury on December 3rd to and including December 5, 1968 as to plaintiffs; Second Cause of Action; and the Court, with the consent of the parties having separated the issues of the existence of the conspiracy alleged by the Trustee and the INDIVIDUAL DEFENDANTS and the commission by SAMUEL BUCHMAN of acts thereunder from the issue of the damages suffered by the Trustee and the INDIVIDUAL DEFENDANTS



JUDGMENT ENTERED OCTOBER 14, 1969

thereform; and the jury having rendered a verdict that SAMUEL BUCHMAN did conspire to injure AMERICAN FOAM RUBBER CORPORATION and the INDIVIDUAL DEFENDANTS and did commit acts in furtherance thereof, as alleged by the Trustee and the INDIVIDUAL DEFENDANTS; and the jury having rendered a verdict under the first counterclaim of defendant ACKMAN in the principal sum of \$20,000.00 in favor of said ACKMAN as against plaintiffs and a verdict that the INDIVIDUAL DEFENDANTS were not damaged by the conspiracy; and the INDIVIDUAL DEFENDANTS' second counterclaim having been withdrawn and discontinued during said trial; and the Court at the conclusion of the evidence at the non-jury phase of the trial having reserved its decision on plaintiffs' Second Cause of Action and thereafter having filed its opinion dated July 23, 1969 holding defendant de MONTMOLLIN liable to plaintiffs and defendants PATHY not liable to them and its opinion dated September 26, 1969 deferring the conclusion of said Second Cause as against de MONTMOLLIN as hereinbelow decreed;

And the Court having filed its two further opinions dated September 26, 1969 holding that defendant ACKMAN is entitled to interest on his recovery of \$20,000.00 and that there should be no set-off as between plaintiffs' and defendant ACKMAN'S recoveries, both as below decreed; it is

JUDGMENT ENTERED OCTOBER 14, 1969

ORDERED and ADJUDGED that plaintiffs have judgment on their First Cause of Action against AMERICAN FOAM RUBBER CORPORATION in the sum of \$64,000.00 with interest thereon at 5% per annum from August 1, 1960 to January 17, 1961 in the amount of \$1,484.47 or in all \$65,484.47 with costs to be taxed in favor of plaintiffs against said AMERICAN FOAM RUBBER CORPORATION and that claim No. 43 of plaintiffs' deceased predecessor, SAMUEL BUCHMAN, filed in the Estate of said AMERICAN FOAM RUBBER CORPORATION, bankrupt, on February 21, 1961 is, subject to all pertinent provisions of the Bankruptcy Act, valid as a general unsecured claim in bankruptcy for said amount of \$65,484.47; and it is further

ORDERED and ADJUDGED that plaintiffs' Second Cause of Action as against defendants ALEXANDER F. PATHY and SUZANNE M. PATHY be and the same hereby is dismissed with costs to be taxed in favor of said defendants against plaintiffs' and it is further

ORDERED and ADJUDGED that defendant MILTON R. ACKMAN as Trustee of AMERICAN FOAM RUBBER CORPORATION, Bankrupt, have judgment on his First Counterclaim against plaintiffs FIRST NATIONAL BANK OF HOLLYWOOD, DOROTHY BUCHMAN and A. SANDER BUCHMAN, as executors of SAMUEL BUCHMAN, deceased, in the sum of \$20,000.00 with interest thereon at 6% per annum from July 1, 1959 to April 29, 1968 in the amount of \$10,593.33 or in all for \$30,593.38



JUDGMENT ENTERED OCTOBER 14, 1969

plus interest thereon at 6% per annum from April 29, 1968 to the date of entry of this judgment in the amount of \$2,651.52, totalling in all \$33,244.65 with costs to be taxed in favor of said defendant ACKMAN against plaintiffs' and it is further

ORDERED and ADJUDGED that plaintiffs' judgment and claim in bankruptcy, mentioned in the first decretal clause above, and defendant ACKMAN'S judgment mentioned in the third decretal clause above shall not be set-off against each other in any part; and it is further

ORDERED and ADJUDGED that defendant ACKMAN'S Second Counterclaim against plaintiff and Cross-Claim against defendants MARIE LOUISE de MONTMOLLIN, ALEXANDER F. PATHY and SUZANNE M. PATHY be and the same hereby is dismissed without costs to plaintiffs and with costs to be taxed in favor of said defendants de MONTMOLLIN and PATHY against said defendant MILTON R. ACKMAN as Trustee of AMERICAN FOAM RUBBER CORPORATION; and it is further

ORDERED and ADJUDGED that the First Counterclaim of defendants MARIE LOUISE de MONTMOLLIN, ALEXANDER F. PATHY and SUZANNE M. PATHY be and the same hereby is dismissed and the Second Counterclaim of said defendants be and the same hereby is discontinued with prejudice, without costs against defendants PATHY and with the liability or non-liability for costs of defendant de MONTMOLLIN reserved as provided in the decretal clause following; and it is further

JUDGMENT ENTERED OCTOBER 14, 1969

ORDERED and ADJUDGED that plaintiffs' Second Cause of Action, referred to in the second decretal clause above, as against defendant de MONTMOLLIN, be and the same hereby is severed, to survive the entry of this judgment and to be disposed of after the conclusion and final windup of the Estate of AMERICAN FOAM RUBBER CORPORATION in bankruptcy, at which time defendant de MONTMOLLIN'S liability, if any, to plaintiffs for costs under said Cause of Action and under her Counterclaims referred to in the preceding decretal clause shall be determined.

DATED: New York, New York  
October 9, 1969

IRVING BEN COOPER  
U.S.D.J.

JUDGMENT ENTERED:

October 9, 1969.



OPINION OF HON. IRVING BEN COOPER, U.S.D.J. DATED  
NOVEMBER 17, 1974.

FIRST NATIONAL BANK OF HOLLYWOOD et al. v. AMERICAN  
FOAM RUBBER CORP., et al. - 60 Civ.2328 (IBC)

The sole issue which must be resolved on this motion for summary judgment is the amount of interest due plaintiff Buchman on the \$15,000 judgment. See our two prior opinions in this case reported under the same caption at 306 F.Supp. 593; 309 F.Supp. 547 (S.D.N.Y. 1969).

New York law governs the question of interest here. Klaxon Co. v. Stentor Electric Mfg. Co., 313 U.S. 487 (1941); Spanos v. Skouras Theatres Corp., 235 F.Supp. 1, 17 (S.D.N.Y. 1964), aff'd, 364 F.2d 161 (2d Cir. 1966). Under New York law, compounding of interest is not allowed unless there is a new promise by the debtor after the interest has accrued. Wolf v. Aero Factors Corp., 126 F.Supp. 872, 881 (S.D.N.Y. 1954), aff'd, 221 F.2d 291 (2d Cir. 1955); Levine v. U.N. Cleaner, 4 A.D. 2d 955, 167 N.Y.S. 2d 801 (2d Dep't 1957). Here there was no new promise or obligation on the debtor's part.

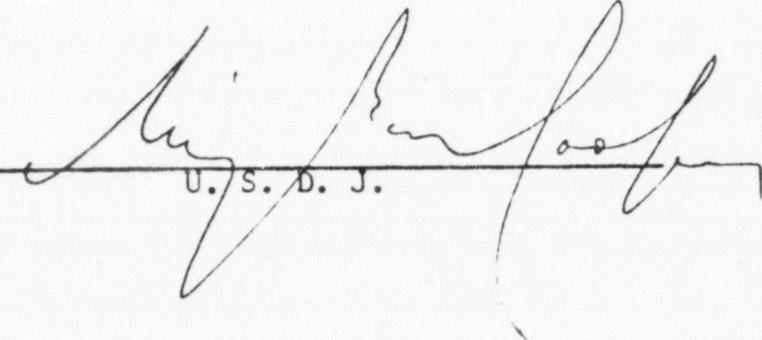
Accordingly, plaintiff should be awarded simple interest on the \$15,000 judgment at the following legal rate: from April 1, 1960 to June 30, 1968 at six per cent per annum; from July 1, 1968 to February 15, 1969 at seven and one quarter per cent per annum; from February 16, 1969 to August 31, 1972 at seven and one half per cent per

OPINION OF HON. IRVING BEN COOPER, U.S.D.J. DATED  
NOVEMBER 17, 1974

annum; and from September 1, 1972 to November 21, 1974  
(date of entry of this order) at six per cent per annum.  
See N.Y. CPLR §§5001, 5004; 3 NYCRR §4.1; Earnest v.  
Donald Deskey Assoc. Inc., 312 F.Supp. 1312 (S.D.N.Y.  
1970). The interest computed by the judgment clerk  
following this formula shall be added to the award of  
\$26,852.58 as to which there is no dispute.

SO ORDERED:

New York, N.Y.  
November 21, 1974

  
U. S. D. J.



JUDGMENT ENTERED DECEMBER 20, 1974.

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

-----x  
FIRST NATIONAL BANK OF HOLLYWOOD,  
DOROTHY BUCHMAN and SANDER BUCHMAN,  
as Executors of Samuel Buchman,  
Deceased,

CIVIL ACTION

No. 60:2328 IBC

Plaintiffs,

- against -

ORDER AND JUDGMENT

AMERICAN FOAM RUBBER CORP., MILTON R.  
ACKMAN, as Trustee of American Foam  
Rubber Corp., Bankrupt, MARIE LOUISE  
de MONTMOLLIN, ALEXANDER F. PATHY and  
SUZANNE M. PATHY,

Defendants.

-----x  
A motion having regularly been made by the plaintiff,  
DOROTHY BUCHMAN, as Executrix of Samuel Buchman, Deceased, above-  
named, for an order for summary judgment pursuant to Rule 56 of  
the Federal Rules of Civil Procedure, in favor of the aforesaid  
plaintiff herein, and the court having considered the affidavit  
of DOROTHY BUCHMAN, sworn to the 4th day of September, 1974 in  
support of the motion, and the affidavit of DAVID SIVE, ESQ.,  
sworn to the 24th day of September, 1974 in opposition thereto,  
and the court having heard the argument of counsel, and due  
deliberation having been had thereon, it is

JUDGMENT ENTERED DECEMBER 20, 1974

ORDERED, that the plaintiff's motion for summary judgment be and the same hereby is granted, and it is therefore

ORDERED, ADJUDGED AND DECREED, that the plaintiff, DOROTHY BUCHMAN, as Executrix of Samuel Buchman, Deceased, recover of the defendant, MARIE LOUISE de MONTMOLLIN, the sum of \$15,000.00 with interest at the following rate per annum from the following dates:

- (a) 6% per annum from April 1, 1960 to June 30, 1968;
- (b) 7 1/4% per annum from July 1, 1968 to February 15, 1969;
- (c) 7 1/2% per annum from February 16, 1969 to August 31, 1972;
- (d) 6% per annum from September 1, 1972 to November 21, 1974,

all of which interest equals the sum of \$14,016.00, and it is further

ORDERED, ADJUDGED AND DECREED, that the plaintiff, DOROTHY BUCHMAN, as Executrix of Samuel Buchman, Deceased, recover of the defendant, MARIE LOUISE de MONTMOLLIN, the additional sum of \$11,514.00 with interest at the rate of 6% per annum from the 21st day of May, 1974 to the 21st day of November, 1974, which interest equals the sum of \$338.58 there-



JUDGMENT ENTERED DECEMBER 20, 1974

by making the total amount to be recovered by the plaintiff,  
DOROTHY BUCHMAN, as Executrix of Samuel Buchman, Deceased, from  
the defendant, MARIE LOUISE de MONTMOLLIN, the sum of \$40,868.58.

Dated: December , 1974

---

United States District Judge

## NOTICE OF APPEAL.

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

-----x  
FIRST NATIONAL BANK OF HOLLYWOOD,  
DOROTHY BUCKMAN and SANDER BUCKMAN, as  
Executors of Samuel Buckman, Deceased,

Plaintiffs,

-against-

AMERICAN FOAM RUBBER CORP., MILTON R.  
ACKMAN, as Trustee of American Foam  
Rubber Corp., Bankrupt, MARIE LOUISE  
de MONTMOLLIN, ALEXANDER F. PATHY and  
SUZANNE M. PATHY,

Defendants.

-----x

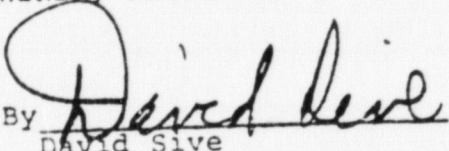
:  
:  
: Civil Action No.  
: 60:2328 IBC

:  
:  
: NOTICE OF APPEAL

NOTICE IS HEREBY GIVEN that defendants MARIE LOUISE de MONTMOLLIN, ALEXANDER F. PATHY and SUZANNE M. PATHY appeal to the United States Court of Appeals for the Second Circuit from the Order and Judgment of the Court, and each and every part thereof, entered in this action on the 20th day of December, 1974, which ordered, adjudged and decreed that plaintiff DOROTHY BUCHMAN, as executrix of Samuel Buchman, recover of defendant MARIE LOUISE de MONTMOLLIN the sum \$40,868.58.

Dated: New York, New York  
January 9, 1975

WINER, NEUBURGER & SIVE

By   
David Sive  
a member of the firm  
Attorney for defendants  
de Montmollin and Pathy



PURCHASE ORDERS CHECKED

263a

NOTICE OF APPEAL

TO:

LOTWIN, GOLDMAN, GUTIN, ROSEN & GREENE,  
Attorneys for Plaintiffs  
540 Madison Avenue  
New York, New York 10022

KLEEBERG & GREENWALD  
Attorneys for Defendant Milton R. Ackman, as Trustee  
East 44th Street  
New York, New York 10017

United States Court of Appeals  
For the Second Circuit

The Reporter Co., Inc., 11 Park Place, New York, N. Y. 10007

First National Bank of Holloywood, Dorothy Buchman  
et al.

Plaintiffs-Appellees

against

American Foam Rubber Corp. et al.

Defendants

Marie Louise et al.

Defendants-Appellants

AFFIDAVIT  
OF SERVICE  
BY MAIL

State of New York, County of New York, ss.:

Raymond J. Braddick, being duly sworn deposes and says that he is  
agent for Winer Neuberger & Sive the attorney  
for the above named Defendants-Appellants herein. That he is over  
21 years of age, is not a party to the action and resides at Levittown, New York

That on the 4th day of April, 1975, he served the within  
Exhibit Volume, Appendix and Brief

Dorothy Buchman  
As Executrix of the Estate of Samuel Buchman Pro Se  
3180 South Ocean Drive  
Hallandale, Florida 33009

upon the attorneys for the parties and at the addresses as specified below

Dorothy Buchman, Executrix of the Estate of Samuel Buchman et al.  
by depositing 3 copies of each

to each of the same securely enclosed in a post-paid wrapper in the Post Office regularly main-  
tained by the United States Government at  
90 Church Street, New York, New York

directed to the said attorneys for the parties as listed above at the addresses aforementioned,

that being the addresses within the state designated by them for that purpose, or the places  
where they then kept offices between which places there then was and now is a regular com-  
munication by mail.

Sworn to before me, this 4th.

day of April, 1975

ROLAND W. JOHNSON  
Notary Public, State of New York  
No. 4509705  
Qualified in Delaware County  
Commission Expires March 30, 1977